

HARTE HANKS INC  
Form 10-K  
March 13, 2013  
[Table of Contents](#)

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

Washington, D.C. 20549

---

**FORM 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2012

**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 001-7120

**HARTE-HANKS, INC.**

Edgar Filing: HARTE HANKS INC - Form 10-K

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**74-1677284**

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

**9601 McAllister Freeway, Suite 610, San Antonio, Texas**  
(Address of principal executive offices)

**78216**  
(Zip Code)

Registrant's telephone number, including area code **210-829-9000**

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

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 if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definitions of large accelerated filer, accelerated filer and small reporting company in Rule 12b-2 of the Exchange Act

Edgar Filing: HARTE HANKS INC - Form 10-K

Large accelerated filer

Accelerated filer

Non-accelerated filer   
(Do not check if a smaller reporting company)

Smaller reporting company

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the closing price (\$9.14) as of the last business day of the registrant's most recently completed second fiscal quarter (June 30, 2012), was approximately \$437,258,000.

The number of shares outstanding of each of the registrant's classes of common stock as of January 31, 2013 was 62,395,489 shares of common stock, all of one class.

---

Table of Contents

**Documents incorporated by reference:**

Portions of the Proxy Statement to be filed for the Company's 2013 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K.

THIS ANNUAL REPORT ON FORM 10-K IS BEING DISTRIBUTED TO STOCKHOLDERS IN LIEU OF A SEPARATE ANNUAL REPORT PURSUANT TO RULE 14a-3(b) OF THE ACT AND SECTION 203.01 OF THE NEW YORK STOCK EXCHANGE LISTED COMPANY MANUAL.

# Edgar Filing: HARTE HANKS INC - Form 10-K

## Table of Contents

Harte-Hanks, Inc. and Subsidiaries

Table of Contents

Form 10-K Report

December 31, 2012

		<b>Page</b>
<u>Part I</u>		
<u>Item 1.</u>	<u>Business</u>	4
<u>Item 1A.</u>	<u>Risk Factors</u>	12
<u>Item 1B.</u>	<u>Unresolved Staff Comments</u>	20
<u>Item 2.</u>	<u>Properties</u>	21
<u>Item 3.</u>	<u>Legal Proceedings</u>	21
<u>Item 4.</u>	<u>Mine Safety Disclosures</u>	21
<u>Part II</u>		
<u>Item 5.</u>	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	21
<u>Item 6.</u>	<u>Selected Financial Data</u>	24
<u>Item 7.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	25
<u>Item 7A.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	41
<u>Item 8.</u>	<u>Financial Statements and Supplementary Data</u>	42
<u>Item 9.</u>	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	42
<u>Item 9A.</u>	<u>Controls and Procedures</u>	42
<u>Item 9B.</u>	<u>Other Information</u>	43
<u>Part III</u>		
<u>Item 10.</u>	<u>Directors, Executive Officers and Corporate Governance</u>	43
<u>Item 11.</u>	<u>Executive Compensation</u>	44
<u>Item 12.</u>	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	44
<u>Item 13.</u>	<u>Certain Relationships and Related Transactions, and Director Independence</u>	44
<u>Item 14.</u>	<u>Principal Accountant Fees and Services</u>	44

Edgar Filing: HARTE HANKS INC - Form 10-K

Part IV  
Item 15.

Exhibits and Financial Statement Schedules

45

Signatures

46

Table of Contents

**PART I**

**ITEM 1. BUSINESS**

**INTRODUCTION**

Harte-Hanks, Inc. (Harte-Hanks) is a worldwide direct and targeted marketing company that provides multichannel direct and digital marketing services and shopper advertising opportunities to a wide range of local, regional, national and international consumer and business-to-business marketers. We manage our operations through two operating segments: Direct Marketing, which operates both nationally and internationally, and Shoppers, which operates in certain California markets.

Virtually all for-profit organizations, as well as many non-profit organizations, rely on marketing to generate revenues and publicity. Many businesses have a chief-level executive responsible for marketing who is charged with combining data, technology, channels and resources to demonstrate a return on marketing investment. This has led many businesses to use direct and targeted marketing, which offer accountability and measurability of marketing programs, allowing customer insight to be leveraged to create and accelerate value. Direct Marketing, which represented 76% of our total revenues in 2012, is a leader in the movement toward highly targeted, multichannel marketing. Our Shoppers business applies geographic targeting principles, providing approximately 780 zones for local marketing.

Harte-Hanks® is the successor to a newspaper business started by Houston Harte and Bernard Hanks in Texas in the early 1920s. In 1972, Harte-Hanks went public and was listed on the New York Stock Exchange (NYSE). We became private in a leveraged buyout initiated by management in 1984. In 1993, we again went public and listed our common stock on the NYSE.

Harte-Hanks provides public access to all reports filed with the Securities and Exchange Commission (SEC) under the Securities Exchange Act of 1934, as amended (the 1934 Act). These documents may be accessed free of charge on our website at <http://www.harte-hanks.com>. These documents are provided as soon as practical after they are filed with the SEC and may also be found at the SEC's website at <http://www.sec.gov>. Additionally, we have adopted and posted on our website a code of ethics that applies to our principal executive officer, principal financial officer and principal accounting officer. Our website also includes our corporate governance guidelines and the charters for each of our audit, compensation, and nominating and corporate governance committees. We will provide a printed copy of any of the aforementioned documents to any requesting stockholder.

**DIRECT MARKETING**

**General**

## Edgar Filing: HARTE HANKS INC - Form 10-K

Our Direct Marketing services offer a wide variety of integrated, multichannel, 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 multichannel 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 and data management software, in media from direct mail to email.

- **Agency & Digital Services.** The Agency Inside Harte-Hanks® and Mason Zimble® are full-service, customer engagement agencies specializing in direct and digital communications for both consumer and business-to-business markets. With strategy, creative and implementation services, we help marketers within targeted industries understand, identify, and engage prospects and customers in their channel of choice. Our digital solutions integrate online services within the marketing mix and include: website development and design, digital strategy, social media marketing and monitoring, email marketing, ecommerce and interactive relationship management and a host of other services that support our core businesses.



Table of Contents

- **Database Marketing Solutions.** We have successfully delivered marketing database solutions for over 35 years across various industries. Our solutions are built around centralized marketing databases with three core offerings: insight and analytics; customer data integration; and marketing communications tools. Our solutions enable organizations to build and manage customer communication strategies that drive new customer acquisition and retention and maximize the value of existing customer relationships. Through insight, we help clients identify models of their most profitable customer relationships and then apply these models to increase the value of existing customers while also winning profitable new customers. Through customer data integration, data from multiple sources comes together to provide a single customer view of client prospects and customers. Then, utilizing our Allink® suite of customer communication and sales optimization tools, we help clients apply their data and insights to the entire customer lifecycle, to help clients sustain and grow their business, gain deeper customer insights, and continuously refine their customer resource management strategies and tactics.
- **Trillium Software® Data Quality and Service Solutions.** Our proprietary software has helped global customers more effectively analyze, enrich, cleanse and report on their product, financial and customer data as part of master data management, data governance, CRM, data warehousing and integration initiatives. With industry-leading Trillium Software System®, Global Locator geocoding product, and associated data governance services, business users can optimize data-based business processes and transactions, realize efficiencies, and enhance the accuracy of their master set of data-improving program results.
- **Business-to-Business Lead Generation.** Our technology marketing solutions provide business-to-business lead generations through our CI Technology Database® and Aberdeen Group®. Our CI Technology Database tracks technology installations, business demographics and over 5 million key decision makers at more than 4.5 million business locations in 25 countries in North America, Latin America, Europe and China. Our clients use the data to gain insight into their prospect's and client's technology buying cycles. Our Aberdeen Group is a provider of fact-based research to identify and educate technology buyers across numerous industries and product categories. Leading technology providers use Aberdeen's proprietary research content for use in their demand creation programs, online marketing campaigns and Web-based sales and marketing tools.
- **Direct Mail and Fulfillment.** As a full-service direct marketing provider and one of the largest mailing partners of the United States Postal Service (USPS®), our operational mandate is to ensure creativity and quality, provide an understanding of the options available in technologies and segmentation strategies and capitalize on economies of scale with our variety of execution options. Our services include digital printing, print on demand, advanced mail optimization, logistics and transportation optimization, tracking (including our proprietary prEtrak® solution), commingling, shrink wrapping and specialized mailings. We also maintain fulfillment centers throughout the United States where we provide custom kitting services, print on demand, product recalls and freight optimization allowing our customers to distribute literature and other marketing materials. With facilities strategically placed nationwide, we are among the largest solo mailers in the country other than the U.S. government.
- **Contact Centers.** We operate teleservice workstations around the globe providing advanced contact center solutions such as: speech, chat, integrated voice response, email, social cloud monitoring and web self-service. We provide both inbound and outbound contact center services and support many languages with our strategically placed global locations for both consumer and business-to-business markets.

Many of our client relationships start with an offering from the list above on an individual solution basis to the client or a combination of our offerings from across our portfolio of businesses. Multichannel marketing is communicating through different marketing solutions or channels, such as email, mobile devices, mail, radio, television, computer, and newspaper, in an integrated form to reach a consumer so it is easy for a consumer to buy in whatever manner the consumer chooses.



Table of Contents

In 2012, 2011 and 2010, Harte-Hanks Direct Marketing had revenues of \$581.1 million, \$614.3 million, and \$601.3 million, respectively, which accounted for approximately 76%, 76%, and 73% of our total revenues, respectively.

**Customers**

Direct marketing services are marketed to specific industries or markets with services and software products tailored to each industry or market. We believe that we are generally able to provide services to new industries and markets by modifying our existing services and applications. We currently provide direct marketing services primarily to the retail, high-tech/telecom, financial services and pharmaceutical/healthcare vertical markets, in addition to a range of selected markets. The largest Direct Marketing client (measured in revenue) comprised 6% of total Direct Marketing revenues in 2012 and 5% of our total revenues in 2012. The largest 25 clients in terms of revenue comprised 42% of total Direct Marketing revenues in 2012 and 32% of our total revenues in 2012.

**Sales and Marketing**

Our enterprise sales force is organized around the five verticals we service: retail, high-tech/telecom, financial services, pharmaceutical/healthcare, and a wide range of selected markets. The enterprise sales force sells a variety of solutions and services to address client's targeted marketing needs. We also maintain solution-specific sales forces and sales groups to sell our individual products and solutions. Our sales forces, with industry-specific knowledge and experience, emphasize the cross-selling of a full range of direct marketing services and are supported by employees in each sector assigned to specific clients. We rely on our enterprise and solution sellers to primarily sell our products and services to new clients and task our employees supporting existing clients to expand our client relationship through additional solutions and products.

**Direct Marketing Facilities**

Direct marketing services are provided at the following facilities, all of which are leased except as otherwise noted:

**National Offices**

Austin, Texas  
Baltimore, Maryland  
Billerica, Massachusetts  
Boston, Massachusetts  
Cincinnati, Ohio  
Deerfield Beach, Florida  
East Bridgewater, Massachusetts  
Fort Worth, Texas  
Fullerton, California

Grand Prairie, Texas  
Jacksonville, Florida  
Maitland, Florida  
Langhorne, Pennsylvania  
Linthicum Heights, Maryland  
New York, New York  
Ontario, California  
San Diego, California  
Shawnee, Kansas  
Texarkana, Texas  
Wilkes-Barre, Pennsylvania  
Yardley, Pennsylvania

**International Offices**

Boeblingen, Germany  
Bristol, United Kingdom  
Frankfurt, Germany  
Hasselt, Belgium owned site  
Madrid, Spain  
Manila, Philippines  
Melbourne, Australia  
São Paulo, Brazil  
Sydney, Australia  
Theale, United Kingdom  
Uxbridge, United Kingdom  
Versailles, France

Table of Contents

**Competition**

Our Direct Marketing business faces competition in all of its offerings and within each of its vertical markets. Direct marketing is a dynamic business, subject to rapid technological change, high turnover of client personnel who make buying decisions, client consolidations, changing client needs and preferences, continual development of competing products and services and an evolving competitive landscape. Our competition comes from numerous local, national and international direct marketing and advertising companies, and client internal resources, against whom we compete for individual projects, entire client relationships and marketing expenditures. Competitive factors in our industry include the quality and scope of services, technical and strategic expertise, the perceived value of the services provided, reputation and brand recognition. We also compete against print and electronic media and other forms of advertising for marketing and advertising dollars in general. Failure to continually improve our current processes, advance and upgrade our technology applications, and to develop new products and services in a timely and cost-effective manner, could result in the loss of our clients or prospective clients to current or future competitors. In addition, failure to gain market acceptance of new products and services could adversely affect our growth. Although we believe that our capabilities and breadth of services, combined with our national and worldwide production capability, industry focus and ability to offer a broad range of integrated services, enable us to compete effectively, our business results may be adversely impacted by competition. Please refer to Item 1A, Risk Factors, for additional information regarding risks related to competition.

**Seasonality**

Our Direct Marketing revenues tend to be higher in the fourth quarter than in other quarters during a given year. This increased revenue is a result of overall increased marketing activity prior to and during the holiday season, primarily related to our retail vertical.

**SHOPPERS**

**General**

Harte-Hanks Shoppers is North America's largest owner, operator and distributor of shopper publications, based on weekly circulation and revenues. Shoppers are weekly advertising publications, 7 by 10 inches in size, distributed free by USPS saturation mail to households and businesses in a particular geographic area. Shoppers offer advertisers a targeted, cost-effective local advertising system, with virtually 100% penetration in its areas of distribution. Shoppers are particularly effective in large markets with high media fragmentation in which major metropolitan newspapers generally have low penetration. Our Shoppers segment also provides online advertising and other services through our website, *PennySaverUSA.com*®, as well as business websites and search engine marketing. Our websites serve as advertising portals, bringing buyers and sellers together through our online offerings, including local classifieds, business listings, coupons, special offers and PowerSites®. PowerSites are templated web sites for our customers, optimized to help small and medium-sized business owners establish a web presence and improve their lead generation through call tracking. At December 31, 2012, we were publishing approximately 5,600 PowerSites weekly.

On December 31, 2012, we sold the assets of our Florida Shoppers operations, The Flyer®, for gross proceeds of \$2.0 million, subject to working capital adjustments. This transaction resulted in an after-tax loss of \$2.7 million. After this sale, Harte-Hanks Shoppers no longer has any operations or circulation in Florida.

## Edgar Filing: HARTE HANKS INC - Form 10-K

Now all of our Shopper operations are located in California, and our California publications account for all Shoppers circulation. As of December 31, 2012, Shoppers delivered approximately 9.1 million shopper packages in six major markets each week, covering Southern, Central and Northern California.

As of December 31, 2012, Harte-Hanks Shoppers published approximately 780 individual shopper editions each week, distributed to zones with circulation of approximately 11,600 in each zone. This allows single-location, local advertisers to saturate a single relevant geographic zone, while enabling multiple-location advertisers to saturate multiple zones. This unique distribution system gives large and small advertisers alike a

Table of Contents

cost-effective way to reach their target markets. Our zoning capabilities and production technologies have enabled us to saturate and target areas in a number of ways, including geographic, demographic, lifestyle, behavioral and language, which we believe allows our advertisers to effectively target their customers. Distribution products are zoned into smaller segments called sub-zones to allow further targeting, primarily for larger accounts targeting specific demographics or store locations; at December 31, 2012 Harte-Hanks offered 2,025 subzones.

In 2012, 2011, and 2010, excluding the Florida Shoppers operations, Harte-Hanks Shoppers had revenues of \$186.6 million, \$197.4 million, and \$219.4 million, respectively, accounting for approximately 24%, 24%, and 27% of our total revenues, respectively.

**Publications**

The following table sets forth certain publication information with respect to Shoppers:

Market	Publication Name	Weekly Circulation	December 31, 2012	
			Zones	Sub-Zones
Greater Los Angeles	<i>PennySaverUSA.com</i>	3,104,082	282	705
Orange County	<i>PennySaverUSA.com</i>	1,054,361	92	270
Inland Empire	<i>PennySaverUSA.com</i>	1,484,720	122	278
San Diego County	<i>PennySaverUSA.com</i>	1,171,601	98	247
Bay Area	<i>PennySaverUSA.com</i>	1,394,632	110	333
Sacramento/Central Valley	<i>PennySaverUSA.com</i>	898,904	79	192
Total		9,108,300	783	2,025

Our shopper publications contain classified and display advertising and are delivered by saturation mail. The typical shopper publication contains approximately 32 pages and is 7 by 10 inches in size. Each edition, or zone, is targeted around a natural neighborhood marketing pattern. Shoppers also serve as a distribution vehicle for national, regional and local advertisers, utilizing print and deliver single-sheet inserts designed and printed by us, four-color glossy flyers designed by us or our customers and printed by third party printers or preprinted customer supplied inserts. During 2012, we distributed approximately 3.9 billion inserted distribution pieces. In addition, our shoppers also provide advertising and other services online through our website, *PennySaverUSA.com*, and our PowerSite product.

We have acquired, developed and applied innovative technology and customized equipment in the publication of our shoppers, contributing to our efficiency. A proprietary pagination system has made it possible for over two thousand zoned editions to be designed, built and output direct-to-plate in a fully digital environment. Automating the production process saves on labor, newsprint and overweight postage. This software also allows for better ad tracking, immediate checks on individual zone and ad status, and more on-time press starts with less manpower.

**Customers**

## Edgar Filing: HARTE HANKS INC - Form 10-K

Shoppers serves both business and individual advertisers in a wide range of industries, including real estate, employment, automotive, retail, grocery, education, telecommunications, financial services, and a number of other industries. The largest client (measured in revenue) comprised 2% of Shoppers revenues in 2012 and less than 1% of our total revenues in 2012. The top 25 clients in terms of revenue comprised 22% of Shoppers revenues in 2012 and 5% of our total revenues in 2012.

### **Sales and Marketing**

We employ more than 270 commissioned sales representatives who develop both targeted and saturation advertising programs, both in print and online, for clients. The sales organization provides service to national, regional and local advertisers through its telemarketing departments and field sales representatives. Shoppers



## Table of Contents

clients vary from individuals with a single item for sale to local neighborhood advertisers to large multi-location advertisers. The weekly number of ads is primarily driven by residential customers, whereas revenues are primarily driven by small and midsize businesses. We also focus our marketing efforts on larger national accounts by emphasizing our ability to deliver saturation advertising in defined zones, or even partial zones for inserts, in combination with advertising in the shopper publication.

Additional focus is placed on particular industries/categories through the use of sales specialists. These sales specialists are primarily used to target automotive, real estate and employment advertisers.

We utilize proprietary sales and marketing systems to enter client orders directly from the field, instantly checking space availability, ad costs and other pertinent information. These systems efficiently facilitate the placement of advertising into multiple-zoned editions and include built-in error-reducing safeguards that aid in minimizing costly sales adjustments. In addition to allowing advertising information to be entered for immediate publication, these systems feed a relational client database, enabling sales personnel to access client history by designated variables to facilitate the identification of similar potential clients and to assist with timely follow-up on existing clients.

## **Shoppers Facilities**

Our shoppers are produced at owned or leased facilities in the markets they serve. At December 31, 2012, we had four production facilities three in Southern California (Brea, Mira Loma and Vista) and one in Northern California (Rancho Cordova). In the third quarter of 2013 the Northern California production facility will be closed, and production of the Northern California publication will be shared among the three Southern California production facilities.

The Southern California production facilities also house our telemarketing sales groups and administrative functions. We also operate several executive suite type offices in areas we serve.

For more information please refer to Item 2, Properties.

## **Competition**

Our Shoppers business competes for advertising, as well as for readers, with other print and electronic media. Competition comes from local and regional newspapers, magazines, radio, broadcast, satellite and cable television, other shoppers, the websites, social media, other communications media and other printed advertising media that operate in our markets. The extent and nature of such competition are, in large part, determined by the location and demographics of the markets targeted by a particular advertiser and the number of media alternatives in those markets. Failure to continually improve our current processes, advance and upgrade our technology applications, and develop new products and services in a timely and cost-effective manner, could result in the loss of our clients to current or future competitors. In addition, failure to gain market acceptance of new products and services, and in geographic areas, could adversely affect our growth. We believe that our production systems and technology, which enable us to publish separate editions in narrowly targeted zones, our local ad content, and our integrated online offering allow us to compete effectively, particularly in large markets with high media fragmentation. However, our business

results may be adversely impacted by competition. Please refer to Item 1A, Risk Factors , for additional information regarding risks related to competition.

**Seasonality**

Historically, the second and third quarters have been the highest revenue quarters for our Shoppers business. Revenues from the last two publication dates in December and the first two to three publication dates in January each year have been affected by a slowdown in advertising by businesses and individuals after the holidays.

Table of Contents

**U.S. AND FOREIGN GOVERNMENT REGULATIONS**

As a company with business activities around the world, we are subject to a variety of domestic and international legal and regulatory requirements that impact our business, including, for example, regulations governing consumer protection and unfair business practices, contracts, ecommerce, intellectual property, labor and employment, securities, tax, and other laws that are generally applicable to commercial activities.

We are also subject to, or affected by, numerous domestic and foreign laws, regulations and industry standards that regulate direct marketing activities, including those that address privacy, data security and unsolicited marketing communications. Examples of some of these laws and regulations that may be applied to, or affect, our business or the businesses of our clients include the following:

- Federal and state laws governing the use of the internet and regulating telemarketing, including the U.S. Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 (CAN-SPAM), which regulates commercial email and requires that commercial emails give recipients an opt-out method. The Canadian Fighting Internet and Wireless Spam Act apply in a comparable manner for our activities in Canada. Telemarketing activities are regulated by, among other requirements, the Federal Trade Commission's Telemarketing Sales Rule (TSR), the Federal Communications Commission's Telephone Consumer Protection Act (TCPA) and various state do-not-call laws.
- The U.S. Department of Commerce's proposed Dynamic Privacy Framework, the Federal Trade Commission's Protecting Consumer Privacy in an Era of Rapid Change policy and the European Commission's proposed changes to the European Union's Data Protection framework, each of which seeks to address consumer privacy, data protection and technological advancements in relation to the collection or use of personal information.
- A significant number of states in the U.S. have passed versions of security breach notification laws, which generally require timely notifications to affected persons in the event of data security breaches or other unauthorized access to certain types of protected personal data.
- The Fair Credit Reporting Act (FCRA), which governs, among other things, the sharing of consumer report information, access to credit scores, and requirements for users of consumer report information.
- The Financial Services Modernization Act of 1999, or Gramm-Leach-Bliley Act (GLB), which, among other things, regulates the use for marketing purposes of non-public personal financial information of consumers that is held by financial institutions. Although Harte-Hanks is not considered a financial institution, many of our clients are subject to the GLB. The GLB also includes rules relating to the physical, administrative and technological protection of non-public personal financial information.
- The Health Insurance Portability and Accountability Act of 1996 (HIPAA), which regulates the use of personal health information for marketing purposes and requires reasonable safeguards designed to prevent intentional or unintentional use or disclosure of protected health information.

- The Fair and Accurate Credit Transactions Act of 2003 (FACT Act), which amended the FCRA and requires, among other things, consumer credit report notice requirements for creditors that use consumer credit report information in connection with risk-based credit pricing actions and also prohibits a business that receives consumer information from an affiliate from using that information for marketing purposes unless the consumer is first provided a notice and an opportunity to direct the business not to use the information for such marketing purposes, subject to certain exceptions.

Table of Contents

- The European Union (EU) data protection laws, including the comprehensive EU Directive on Data Protection (1995), which imposes a number of obligations with respect to use of personal data, and includes a prohibition on the transfer of personal information from the EU to other countries that do not provide consumers with an adequate level of privacy or security. The EU standard for adequacy is generally stricter and more comprehensive than that of the U.S. and most other countries.

There are additional consumer protection, privacy and data security regulations in the U.S. and in other countries in which we or our clients do business. These laws regulate the collection, use, disclosure and retention of personal data and may require consent from consumers and grant consumers other rights, such as the ability to access their personal data and to correct information in the possession of data controllers. We and many of our clients also belong to trade associations that impose guidelines that regulate direct marketing activities, such as the Direct Marketing Association's Commitment to Consumer Choice.

As a result of increasing public awareness and interest in individual privacy rights, data protection, information security and environmental and other concerns regarding marketing communications, federal, state and foreign governmental and industry organizations continue to consider new legislative and regulatory proposals that would impose additional restrictions on direct marketing services and products. Examples include data encryption standards, data breach notification requirements, consumer choice and consent restrictions and increased penalties against offending parties, among others. In 2012, several members of the U.S. Congress (in coordination with the Federal Trade Commission and consumer advocacy groups) initiated several inquiries regarding data brokerage, one of which was directed to us (among others). We anticipate that additional inquiries will be made, and that proposals will continue to be introduced in the future, some of which may be adopted.

In addition, our business may be affected by the impact of these restrictions on our clients and their marketing activities. These additional regulations could increase compliance requirements and restrict or prevent the collection, management, aggregation, transfer, use or dissemination of information or data that is currently legally available. Additional regulations may also restrict or prevent current practices regarding unsolicited marketing communications. For example, many states have considered implementing do-not-mail legislation that could impact our Direct Marketing and Shoppers businesses and the businesses of our clients and customers. In addition, continued public interest in individual privacy rights and data security may result in the adoption of further voluntary industry guidelines that could impact our direct marketing activities and business practices.

We cannot predict the scope of any new legislation, regulations or industry guidelines or how courts may interpret existing and new laws. Additionally, enforcement priorities by governmental authorities may change and also impact our business either directly or through requiring our customers to alter their practices. Compliance with regulations is costly and time-consuming for us and our clients, and we may encounter difficulties, delays or significant expenses in connection with our compliance. We may also be exposed to significant penalties, liabilities, reputational harm and loss of business in the event that we fail to comply with applicable regulations. There could be a material adverse impact on our business due to the enactment or enforcement of legislation or industry regulations, the issuance of judicial or governmental interpretations, enforcement priorities of governmental agencies or a change in customs arising from public concern over consumer privacy and data security issues.

**INTELLECTUAL PROPERTY RIGHTS**

Our intellectual property assets include trademarks and service marks that identify our company and our products and services, software and other technology that we develop, our proprietary collections of data and intellectual property licensed from third parties, such as prospect list providers. We generally seek to protect our intellectual property through a combination of license agreements and trademark, service mark, copyright,



Table of Contents

patent and trade secret laws, and domain name registrations and enforcement procedures. We also enter into confidentiality agreements with many of our employees, vendors and clients and seek to limit access to and distribution of intellectual property and other proprietary information. We pursue the protection of our trademarks and other intellectual property in the United States and internationally.

Despite our efforts to protect our intellectual property, unauthorized parties may attempt to copy or otherwise obtain and use our proprietary information and technology. Monitoring unauthorized use of our intellectual property is difficult, and unauthorized use of our intellectual property may occur. We cannot be certain that patents or trademark registrations will be issued, nor can we be certain that any issued patents or trademark registrations will give us adequate protection from competing products. For example, issued patents may be circumvented or challenged and declared invalid or unenforceable. In addition, others may develop competing technologies or databases on their own. Moreover, there is no assurance that our confidentiality agreements with our employees or third parties will be sufficient to protect our intellectual property and proprietary information.

We may also be subject to infringement claims against us by third parties and may incur substantial costs and devote significant management resources in responding to such claims. We are obligated under some agreements to indemnify our clients as a result of claims that we infringe on the proprietary rights of third parties. These costs and diversions could cause our business to suffer. If any party asserts an infringement claim, we may need to obtain licenses to the disputed intellectual property. We cannot assure you, however, that we will be able to obtain these licenses on commercially reasonable terms or that we will be able to obtain any licenses at all. The failure to obtain necessary licenses or other rights may have an adverse affect on our ability to provide our products and services.

**EMPLOYEES**

As of December 31, 2012, Harte-Hanks employed approximately 6,140 full-time employees and 270 part-time employees, of which approximately 2,040 are based outside of the U.S. Approximately 5,210 full-time and 70 part-time employees were in the Direct Marketing segment and 910 full-time and 200 part-time employees were in the Shoppers segment. A portion of our workforce is provided to us through staffing companies. None of the workforce is represented by labor unions. We consider our relations with our employees to be good.

**ITEM 1A. RISK FACTORS**

**Cautionary Note Regarding Forward-Looking Statements**

This report, including the 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 (1933 Act) and Section 21E of the Securities Exchange Act of 1934 (1934 Act). 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, could, intends, or words of similar meaning. Examples include, but are not limited to, regarding (1) our strategies and initiatives, (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

## Edgar Filing: HARTE HANKS INC - Form 10-K

for our businesses and for the industries in which we operate, including with regard to the performance trends in our Shoppers business and the impact of economic conditions in the United States and other markets we serve on the marketing expenditures and activities of our Direct Marketing clients and prospects, (5) competitive factors, (6) acquisition and development plans, (7) our stock repurchase program, (8) expectations regarding legal proceedings and other contingent liabilities, and (9) other statements regarding future events, conditions or outcomes.



Table of Contents

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 SEC, including the factors discussed below in this Item 1A, **Risk Factors**, and any updates thereto in our Forms 10-Q. 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.

In addition to the information set forth elsewhere in this report, including in the MD&A section, the factors described below should be considered carefully in making any investment decisions with respect to our securities. The risks described below are not the only ones we face or may face in the future. Additional risks and uncertainties that are not presently anticipated or that we may currently believe are immaterial could also impair our business operations and financial performance.

***We face significant competition for individual projects, entire client relationships and advertising dollars in general.***

Our Direct Marketing business faces significant competition in all of its offerings and within each of its vertical markets. Direct marketing is a dynamic business, subject to rapid technological change, high turnover of client personnel who make buying decisions, client consolidations, changing client needs and preferences, continual development of competing products and services and an evolving competitive landscape. This competition comes from numerous local, national and international direct marketing and advertising companies, and client internal resources, against whom we compete for individual projects, entire client relationships and marketing expenditures by clients and prospective clients. We also compete against print and electronic media and other forms of advertising for marketing and advertising dollars in general. In addition, our ability to attract new clients and to retain existing clients may, in some cases, be limited by clients' policies on or perceptions of conflicts of interest. These policies can prevent us from performing similar services for competing products or companies. Our Shoppers business competes for advertising, as well as for readers, with other print and electronic media. Competition comes from local and regional newspapers, magazines, radio, broadcast, satellite and cable television, other shoppers, the internet, other communications media and other advertising printers that operate in our markets. The extent and nature of such competition are, in large part, determined by the location and demographics of the markets targeted by a particular advertiser and the number of media alternatives in those markets. Our failure to improve our current processes or to develop new products and services could result in the loss of our clients to current or future competitors. In addition, failure to gain market acceptance of new products and services could adversely affect our growth.

***Current and future competitors may have significantly greater financial and other resources than we do, and they may sell competing products and services at lower prices or at lower profit margins, resulting in pressures on our prices and margins.***

The sizes of our competitors vary widely across market and service segments. Therefore, some of our competitors may have significantly greater financial, technical, marketing or other resources than we do in one or more of our market segments, or overall. As a result, our competitors may be in a position to respond more quickly than we can to new or emerging technologies and changes in customer requirements, or may devote greater resources than we can to the development, promotion, sale and support of products and services. Moreover, new competitors or alliances among our competitors may emerge and potentially reduce our market share, revenue or margins. Some of our competitors also may choose to sell products or services competitive to ours at lower prices by accepting lower margins and profitability, or may be able to sell products or services competitive to ours at lower prices given proprietary ownership of data, technical superiority or economies of scale. Price reductions or pricing pressure by our competitors could negatively impact our margins and results.



Table of Contents

of operations, and could also harm our ability to obtain new customers on favorable terms. Competitive pricing pressures tend to increase in difficult economic environments, such as the current environments in the United States and other economies, due to reduced marketing expenditures of many of our clients and prospects and the resulting impact on the competitive business environment for marketing service providers such as our company.

***We must maintain technological competitiveness, continually improve our processes and develop and introduce new products and services in a timely and cost-effective manner.***

We believe that our success depends on, among other things, maintaining technological competitiveness in our Direct Marketing and Shoppers products, processing functionality and software systems and services. Technology changes rapidly and there are continuous improvements in computer hardware, network operating systems, programming tools, programming languages, operating systems, database technology and the use of the internet. Advances in information technology may result in changing client preferences for products and product delivery formats in our industry. We must continually improve our processes and provide new products and services in a timely and cost-effective manner through development, license or acquisition to match our competitors' technological developments and competing product/service offerings, and to satisfy the increasingly sophisticated requirements of our clients. We may be unable to successfully identify, develop and bring new and enhanced services and products to market in a timely and cost-effective manner, such services and products may not be commercially successful, and services, products and technologies developed by others may render our services and products noncompetitive or obsolete.

***Our success depends on our ability to consistently and effectively deliver our products and services to our clients.***

Our success depends on our ability to effectively and consistently staff and execute client engagements within the agreed upon timeframe and budget. Depending on the needs of our clients, our Direct Marketing engagements may require customization, integration and coordination of a number of complex product and service offerings and execution across many of our facilities worldwide. Moreover, in some of our engagements, we rely on subcontractors and other third parties to provide a portion of our overall services, and we cannot guarantee that these third parties will effectively deliver their services or that we will have adequate recourse against these third parties in the event they fail to effectively deliver their services. Other contingencies and events outside of our control may also impact our ability to provide our products and services. Our failure to effectively and timely staff, coordinate and execute our client engagements may adversely impact existing client relationships, the amount or timing of payments from our clients, our reputation in the marketplace and ability to secure additional business and our resulting financial performance. In addition, our contractual arrangements with our Direct Marketing clients and other customers may not provide us with sufficient protections against claims for lost profits or other claims for damages.

***If our new leaders are unsuccessful, or if we lose key management and are unable to attract and retain the talent required for our business, our operating results could suffer.***

Our prospects depend in large part upon our ability to attract, train and retain experienced technical, client services, sales, consulting, research and development, marketing, administrative and management personnel. While the demand for personnel is dependent on employment levels, competitive factors and general economic conditions, qualified personnel historically have been in great demand. The loss or prolonged absence of the services of these individuals could have a material adverse effect on our business, financial position or operating results. In addition, we have recently replaced the leaders of our Direct Marketing and Shoppers divisions, and reorganized our operational structures. If our new leaders fail to successfully adapt to their new roles and responsibilities in our reorganized business and more generally if we are unable to attract new leaders with the necessary skills to manage our business our business and its operating results may suffer.



Table of Contents

***We have recently experienced, and may experience in the future, reduced demand for our products and services and increased bad debt expense because of general economic conditions, the financial conditions and marketing budgets of our clients and other factors that may impact the industry verticals that we serve.***

Economic downturns and turmoil severely affect the marketing services industry. Throughout the most recent recession, as in prior economic downturns, our customers responded to weak economic conditions by reducing their marketing budgets, which are generally discretionary in nature and easier to reduce in the short-term than other expenses. Our customers may be slow to restore their marketing budgets to prior levels during a recovery, and may respond similarly to adverse economic conditions in the future. In addition, revenues from our Shoppers business are largely dependent on local advertising expenditures in the markets in which they operate. Such expenditures are substantially affected by the strength of the local economies in those markets. Direct Marketing revenues are dependent on national, regional and international economies and business conditions. A lasting economic recession or anemic recovery in the U.S. or other markets in which we operate (such as the recent recession and recovery) could have material adverse effects on our business, financial position or operating results. Similarly, industry or company-specific factors may negatively impact our clients and prospective clients or their industries, and in turn result in reduced demand for our products and services, client insolvencies, collection difficulties or bankruptcy preference actions related to payments received from our clients. We may also experience reduced demand as a result of consolidation of clients and prospective clients in the industry verticals that we serve. See Management's Discussion and Analysis of Financial Condition and Results of Operations in this Form 10-K for additional information about the adverse impact on our financial performance of the ongoing difficult economic environment in the United States and other economies.

***Our Shoppers business is geographically concentrated and is greatly affected by the California economy.***

Our Shoppers business is concentrated exclusively in California. An economic downturn in California (such as the recent downturn), an anemic recovery (such as the present recovery), or a large disaster (such as a flood, hurricane, earthquake or other disaster or condition that disables our facilities, immobilizes the USPS or causes a significant negative change in the economy of California or the individual markets we serve) could have a material adverse effect on our business, financial position or operating results.

***Our business plan requires us to effectively manage our costs. If we do not achieve our cost management objectives, our financial results could be adversely affected.***

Our business plan and expectations for the future require that we effectively manage our cost structure, including our operating expenses and capital expenditures across our operations. To the extent that we do not effectively manage our costs, our financial results may be adversely affected in any economic climate and even more so during a prolonged recession, such as the recent economic downturn in the United States and elsewhere.

***Privacy, information security and other direct marketing regulatory requirements may prevent or impair our ability to offer our products and services.***

We are subject to and affected by numerous laws, regulations and industry standards that regulate direct marketing activities, including those that address privacy, data protection, information security and marketing communications. Please refer to the section above entitled "U.S. and

## Edgar Filing: HARTE HANKS INC - Form 10-K

Foreign Government Regulations for additional information regarding some of these regulations.

As a result of increasing public awareness and interest in privacy rights, data protection and access, information security, environmental protection and other concerns, national and local governments and industry organizations regularly consider and adopt new laws, rules, regulations and guidelines that restrict or regulate marketing communications, services and products. Examples include data encryption standards, data breach notification requirements, registration/licensing requirements (often with fees), consumer choice, notice and consent restrictions and penalties for infractions, among others. We anticipate that additional restrictions and regulations will continue to be proposed and adopted in the future.

Table of Contents

In addition, our business may be affected by the impact of these restrictions and regulations on our clients and their marketing activities. Current and future restrictions and regulations could increase compliance requirements and costs, and restrict or prevent the collection, management, aggregation, transfer, use or dissemination of information, or change the requirements therefore so as to require other changes to our business or that of our clients. Additional restrictions and regulations may limit or prohibit current practices regarding marketing communications. For example, many states and countries have considered implementing do not contact legislation that could impact our Direct Marketing and Shoppers businesses and the businesses of our clients and customers. In addition, continued public interest in privacy rights, data protection and access, and information security may result in the adoption of further industry guidelines that could impact our direct marketing activities and business practices.

We cannot predict the scope of any new laws, rules, regulation or industry guidelines or how courts or agencies may interpret current ones. Additionally, enforcement priorities by governmental authorities will change over time, which may impact our business. Understanding the laws, rules, regulations and guidelines applicable to specific client multichannel engagements and across many jurisdictions poses a significant challenge, as such laws, rules, regulations and guidelines are often inconsistent or conflicting, and are sometimes at odds with client objectives. Our failure to properly comply with these regulatory requirements and client needs may materially and adversely affect our business. General compliance with privacy, data protection and information security obligations is costly and time-consuming, and we may encounter difficulties, delays or significant expenses in connection with our compliance. We may be exposed to significant penalties, liabilities, reputational harm and loss of business in the event that we fail to comply. We could suffer a material adverse impact on our business due to the enactment or enforcement of legislation or industry regulations, the issuance of judicial or governmental interpretations, changed enforcement priorities of governmental agencies or a change in behavior arising from public concern over privacy, data protection and information security issues.

***We could fail to adequately protect our intellectual property rights and may face claims for intellectual property infringement.***

Our ability to compete effectively depends in part on the protection of our technology, products, services and brands through intellectual property right protections, including patents, copyrights, database rights, trade secrets, trademarks and domain name registrations and enforcement procedures. The extent to which such rights can be protected and enforced varies in different jurisdictions. Litigation involving patents and other intellectual property rights has become far more common and expensive in recent years, and we face the risk of additional litigation relating to our use or future use of intellectual property rights of third parties. Third-party infringement claims and any related litigation against us could subject us to liability for damages, significantly increase our costs, restrict us from using and providing our technologies, products or services or operating our business generally, or require changes to be made to our technologies, products and services. Please refer to the section above entitled **Intellectual Property Rights** for additional information regarding our intellectual property and associated risks.

***Consumer perceptions regarding the privacy and security of their data may prevent or impair our ability to offer our products and services.***

Various federal, state, foreign and industry regulations give consumers varying degrees of control as to how certain data regarding them is collected, used and shared for marketing purposes. If, due to privacy, security or other concerns, consumers exercise their ability to prevent or limit such data collection, use or sharing, it may impair our ability to provide direct marketing to those consumers and limit our clients requirements for our services. Additionally, privacy and security concerns may limit consumers willingness to voluntarily provide data to our customers or marketing companies. Some of our services depend on voluntarily provided data and may be impaired without such data.

Table of Contents

***Our reputation and business results may be adversely impacted if we, or subcontractors upon whom we rely, do not effectively protect sensitive personal information of our clients and our clients' customers.***

Current privacy and data security laws and industry standards impact the manner in which we capture, handle, analyze and disseminate customer and prospect data as part of our client engagements. In many instances, client contracts also mandate privacy and security practices. If we fail to effectively protect and control sensitive personal information (such as personal health information, social security numbers or credit card numbers) of our clients and their customers or prospects in accordance with these requirements, we may incur significant expense, suffer reputational harm and loss of business, and, in certain cases, be subjected to regulatory or governmental sanctions or litigation. These risks may be increased due to our reliance on subcontractors and other third parties in providing a portion of our overall services in certain engagements. We cannot guarantee that these third parties will effectively protect and handle sensitive personal information or other confidential information, or that we will have adequate recourse against these third parties in that event.

***We may not be able to adequately protect our information systems.***

Our ability to protect our information systems against damage from a data loss, security breach, human error, malfeasance, computer virus, fire, power loss, telecommunications failure or other disaster is critical to our future success. Some of these systems may be outsourced to third-party providers from time to time. Any damage to our information systems that causes interruptions in our operations or a loss of data could affect our ability to meet our clients' requirements, which could have a material adverse effect on our business, financial position or operating results. While we take precautions to protect our information systems, such measures may not be effective, and existing measures may become inadequate because of changes in future conditions. Although we maintain insurance which may respond to cover some types of damages incurred by breaches of (or problems with) our information systems, such insurance is limited and expensive, and may not respond or be sufficient to prevent such damage from materially harming our business.

***Breaches of security, or the perception that ecommerce is not secure, could severely harm our business and reputation.***

Business-to-business and business-to-consumer electronic commerce requires the secure transmission of confidential information over public networks. Some of our products and services are accessed through the internet. Security breaches in connection with the delivery of our products and services, or well-publicized security breaches that may affect us or our industry, such as database intrusion, could be severely detrimental to our business, operating results and financial condition. We cannot be certain that advances in criminal capabilities, new discoveries in the field of cryptography or other developments will not compromise or breach the technology protecting the information systems that access our products, services and proprietary database information.

***Data suppliers could withdraw data that we rely on for our products and services.***

We purchase or license much of the data we use. There could be a material adverse impact on our Direct Marketing business if owners of the data we use were to withdraw or cease to allow access to the data or materially restrict the authorized uses of their data. Data providers could withdraw their data if there is a competitive reason to do so, if there is pressure from the consumer community or if additional legislation is passed restricting the use of the data. We also rely upon data from other external sources to maintain our proprietary and non-proprietary databases, including data received from customers and various government and public record sources. If a substantial number of data providers



or other key data sources were to withdraw or restrict their data, if we were to lose access to data due to government regulation, or if the collection of data becomes uneconomical, our ability to provide products and services to our clients could be materially adversely affected, which could result in decreased revenues, net income and earnings per share.

*We must successfully evaluate acquisition targets and integrate acquisitions.*

We frequently evaluate acquisition opportunities to expand our product and service offerings and geographic locations, including potential international acquisitions. Acquisition activities, even if not consummated, require substantial amounts of management time and can distract from normal operations. In addition, we may

Table of Contents

be unable to achieve the profitability goals, synergies and other objectives initially sought in acquisitions, and any acquired assets, data or businesses may not be successfully integrated into our operations. Acquisitions may result in the impairment of relationships with employees and customers. Moreover, although we review and analyze assets or companies we acquire, such reviews are subject to uncertainties and may not reveal all potential risks, and we may incur unanticipated liabilities and expenses as a result of our acquisition activities. The failure to identify appropriate candidates, to negotiate favorable terms, or to successfully integrate future acquisitions into existing operations could result in not achieving planned revenue growth and could negatively impact our net income and earnings per share.

***We are vulnerable to increases in paper prices.***

Newsprint prices are subject to fluctuations. We maintain, on average, less than 75 days of paper inventory for our Shoppers business and do not purchase our paper pursuant to long-term paper contracts. Because we have a limited ability to protect ourselves from increases in the price of paper or to pass increased costs along to our clients, these increases could materially affect the results of our operations. Likewise, increased paper costs could also cause our Direct Marketing customers to reduce spending on other marketing programs, or to shift to media which are less profitable for us, in each case potentially materially affecting our revenues and profits.

***We are vulnerable to increases in postal rates and disruptions in postal services.***

Our Shoppers and Direct Marketing services depend on the USPS and other commercial delivery services to deliver products. Our Shoppers are delivered by saturation mail, and postage is the largest expense in our Shoppers business. Standard postage rates have increased in recent years (most recently in April 2011, January 2012 and January 2013) and may continue to do so at frequent and unpredictable intervals. Shoppers postage rates increased by less than 1.0% as a result of the April 2011 rate increase, increased by approximately 2.1% as a result of the January 2012 rate increase, and will increase by approximately 2.8% as a result of the January 2013 rate increase. The January 2013 postage rate increase, and any additional future changes in postage rates will affect Shoppers' distribution costs. Postage rates also influence the demand for our Direct Marketing services even though the cost of mailings is typically borne by our clients and is not directly reflected in our revenues or expenses. Accordingly, future postal increases or disruptions in the operations of the USPS may have an adverse impact on us.

The USPS has had significant financial and operational challenges recently. In reaction, the USPS has proposed many changes in its services, such as delivery frequency and facility access. Recently, the USPS announced it would end household delivery on Saturdays starting in August 2013. At this point we do not believe the announced or proposed changes will have a material impact on our business. Additional changes, individually or in combination with other market factors, could materially and negatively affect our costs and ability to meet our clients' expectations.

***Our financial results could be negatively impacted by impairments of goodwill or other intangible assets with indefinite useful lives.***

In the second quarter of 2012 we recorded an impairment charge of \$165.3 million related to goodwill and other intangible assets in our Shoppers business as a result of continuing revenue declines, the poor economic conditions in the geographies in which we operated, and management's evaluation of the business. Excluding the Florida Shoppers operations (which were sold at the end of 2012 and are included in discontinued operations), the total impairment charge related to our Shoppers business was \$156.9 million. As of December 31, 2012, the net book value of our goodwill and other intangibles represented approximately \$414.0 million out of our total assets of \$706.2 million. We

## Edgar Filing: HARTE HANKS INC - Form 10-K

continue to test goodwill and other intangible assets with indefinite useful lives for impairment as of November 30 of each year and on an interim date should factors or indicators become apparent that would require an interim test. A downward revision in the fair value of either of our reporting units or any of the other intangible assets could result in additional impairments and non-cash charges. Any such impairment charges could have a significant negative effect on our reported net income.

Table of Contents

*Our indebtedness may adversely impact our ability to react to changes in our business or changes in general economic conditions.*

The amount of our indebtedness and the terms under which we have borrowed money under our credit facilities or other agreements could have important consequences for our business. Our debt covenants require that we maintain certain financial measures and ratios. As a result of these covenants and ratios, we may be limited in the manner in which we can conduct our business, and we may be unable to engage in favorable business activities or finance future operations or capital needs. A failure to comply with these restrictions or to maintain the financial measures and ratios contained in the debt agreements could lead to an event of default that could result in an acceleration of outstanding indebtedness. In addition, the amount and terms of our indebtedness could:

- limit our flexibility in planning for, or reacting to, changes in our business and the industries in which we operate, including limiting our ability to invest in our strategic initiatives, and, consequently, place us at a competitive disadvantage;
- reduce the availability of our cash flows that would otherwise be available to fund working capital, capital expenditures, acquisitions and other general corporate purposes; and
- result in higher interest expense in the event of increases in interest rates, as discussed below under Interest rate increases could affect our results of operations, cash flows and financial position.

We may incur additional indebtedness in the future and, if new debt is added to our current debt levels, the above risks could be increased.

*Interest rate increases could affect our results of operations, cash flows and financial position.*

Interest rate movements in Europe and the United States can affect the amount of interest we pay related to our debt and the amount we earn on cash equivalents. Our primary interest rate exposure is to interest rate fluctuations in Europe, specifically Eurodollar rates, due to their impact on interest related to our credit facilities. As of December 31, 2012, we had \$110.3 million of debt outstanding, all of which bore variable interest rates. Our results of operations, cash flows and financial position could be materially adversely affected by significant increases in interest rates. We also have exposure to interest rate fluctuations in the United States, specifically money market, commercial paper and overnight time deposit rates, as these affect our earnings on excess cash. Even with the offsetting increase in earnings on excess cash in the event of an interest rate increase, we cannot be assured that future interest rate increases will not have a material adverse impact on our business, financial position or operating results.

*Our international operations subject us to risks associated with operations outside the U.S.*

## Edgar Filing: HARTE HANKS INC - Form 10-K

Harte-Hanks Direct Marketing conducts business outside of the United States. During 2012, approximately 15.3% of Harte-Hanks Direct Marketing's revenues and 11.6% of Harte-Hanks total revenues were derived from operations outside the United States, primarily Europe, Asia and South America. We may expand our international operations in the future as part of our growth strategy. Accordingly, our future operating results could be negatively affected by a variety of factors, some of which are beyond our control, including:

- social, economic and political instability;
- changes in U.S. and foreign governmental legal requirements or policies resulting in burdensome government controls, tariffs, restrictions, embargoes or export license requirements;
- inflation;
- the potential for nationalization of enterprises;
- less favorable labor laws that may increase employment costs and decrease workforce flexibility;
- potentially adverse tax treatment;
- less favorable foreign intellectual property laws that would make it more difficult to protect our intellectual properties from appropriation by competitors;
- more onerous or differing data privacy and security requirements or other marketing regulations;
- longer payment cycles for sales in foreign countries; and
- the costs and difficulties of managing international operations.

Table of Contents

In addition, exchange rate movements may have an impact on our future costs or on future cash flows from foreign investments. We have 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. The various risks that are inherent in doing business in the United States are also generally applicable to doing business outside of the United States, and may be exaggerated by the difficulty of doing business in numerous sovereign jurisdictions due to differences in culture, laws and regulations.

*We must maintain effective internal controls.*

In designing and evaluating our internal controls over financial reporting, we recognize that any internal control or procedure, no matter how well designed and operated, can provide only reasonable assurance of achieving desired control objectives and that no system of internal controls can be designed to provide absolute assurance of effectiveness. If we fail to maintain a system of effective internal controls, it could have a material adverse effect on our business, financial position or operating results. Additionally, adverse publicity related to a failure in our internal controls over financial reporting could have a negative impact on our reputation and business.

*Fluctuation in our revenue and operating results and other factors may impact the volatility of our stock price.*

The price at which our common stock has traded in recent years has fluctuated greatly and has declined significantly. Our common stock price may continue to be volatile due to a number of factors including the following (some of which are beyond our control):

- the impact and duration of the ongoing economic downturn, overall strength of the United States and other economies and general market volatility;
- variations in our operating results from period to period and variations between our actual operating results and the expectations of securities analysts, investors and the financial community;
- unanticipated developments with client engagements or client demand, such as variations in the size, budget, or progress toward the completion of engagements, variability in the market demand for our services, client consolidations and the unanticipated termination of several major client engagements;
- announcements of developments affecting our businesses;
- competition and the operating results of our competitors; and
- other factors discussed elsewhere in this Item 1A, Risk Factors .

As a result of these and other factors, investors in our common stock may not be able to resell their shares at or above their original purchase price.

*War or terrorism could affect our business.*

War and/or terrorism or the threat of war and/or terrorism involving the United States could have a significant impact on our business, financial position or operating results. War or the threat of war could substantially affect the levels of advertising expenditures by clients in each of our businesses, whether due to economic declines, reactions to security risks or other factors. In addition, each of our businesses could be affected by operation disruptions and a shortage of supplies and labor related to such a war or threat of war.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

Table of Contents

**ITEM 2. PROPERTIES**

Our headquarters are located in San Antonio, Texas, and we occupy approximately 8,000 square feet of leased office space at that location. Our business is conducted in facilities worldwide containing aggregate space of approximately 2.8 million square feet. Approximately 2.6 million square feet are held under leases, which expire at dates through 2020. The balance of our properties, used in our Brea, California Shoppers operations and Hasselt, Belgium Direct Marketing operations, are owned.

**ITEM 3. LEGAL PROCEEDINGS**

Information regarding legal proceedings is set forth in Note J, *Commitments and Contingencies*, of the Notes to Consolidated Financial Statements and is incorporated herein by reference.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable

**PART II**

**ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

**Common Stock**

Our common stock is listed on the NYSE (symbol: HHS). The reported high and low quarterly sales price ranges for 2012 and 2011 were as follows:

	2012		2011	
	High	Low	High	Low
First Quarter	10.24	8.30	13.74	11.77
Second Quarter	9.25	8.05	12.22	7.59
Third Quarter	9.81	6.16	8.95	7.00
Fourth Quarter	7.02	5.14	9.94	7.74



## Edgar Filing: HARTE HANKS INC - Form 10-K

We paid a quarterly dividend of 8.5 cents per share in each of the first three quarters of 2012 and two dividends of 8.5 cents per share in the fourth quarter of 2012. The second dividend paid in the fourth quarter of 2012 was a one-time acceleration of the regular quarterly dividend we would have ordinarily paid in the first quarter of 2013. As a result, we do not anticipate paying a dividend in the first quarter of 2013. We currently plan to pay a quarterly dividend of 8.5 cents per share in each of the second, third and fourth quarters of 2013, although any actual dividend declaration can be made only upon approval of our Board of Directors, based on its business judgment.

In 2011, quarterly dividends were paid at the rate of 8.0 cents per share.

As of January 31, 2013, there are approximately 2,130 holders of record.

Table of Contents**Issuer Purchases of Equity Securities**

The following table contains information about our purchases of equity securities during the fourth quarter of 2012:

<b>Period</b>	<b>Total Number of Shares Purchased(2)</b>	<b>Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of a Publicly Announced Plan(1)</b>	<b>Maximum Dollar Amount that May Yet Be Spent Under the Plan</b>
October 1 31, 2012	94,063	\$ 6.96	90,000	\$ 7,334,604
November 1 30, 2012	0	\$ 0	0	\$ 7,334,604
December 1 31, 2012	297,378	\$ 5.84	297,378	\$ 5,597,033
Total	391,441	\$ 6.11	387,378	

(1) During the fourth quarter of 2012, we purchased 387,378 shares of our common stock through our stock repurchase program that was publicly announced in August 2012. Under this program, from which shares can be purchased in the open market, our Board of Directors has authorized us to spend up to \$10.0 million to repurchase shares of our outstanding common stock. As of December 31, 2012, we have repurchased 700,284 shares and spent \$4.6 million under this authorization. Through December 31, 2012, we had repurchased a total of 65,602,625 shares at an average price of \$18.55 per share under this program and previously announced programs.

(2) Total number of shares purchased includes shares, if any, purchased as part of our publicly announced stock repurchase program, plus shares withheld to pay applicable withholding taxes and the exercise price related to stock options, and shares withheld to pay applicable withholding taxes related to the vesting of nonvested shares, pursuant to the Harte-Hanks, Inc. 2005 Omnibus Incentive Plan.

**Comparison of Stockholder Returns**

*The material under this heading is not soliciting material, is not deemed filed with the SEC, and is not to be incorporated by reference into any filing under the 1933 Act or the 1934 Act, whether made before or after the date hereof and irrespective of any general incorporation language in such filing.*

The following graph compares the cumulative total return of our common stock during the period December 31, 2007 to December 31, 2012 with the Standard & Poor's 500 Stock Index (S&P 500 Index) and with our peer group.

Our peer group includes Acxiom Corporation, Alliance Data Systems Corporation, Cenveo, Inc., Consolidated Graphics, Inc., Convergys Corp., Dun & Bradstreet Corporation, Equifax, Inc., Gartner, Inc., Informatica Corp., Interpublic Group of Companies, Inc., Meredith Corp., Sapient Corp., Sykes Enterprises, Inc., Techtarget, Inc., Valassis Communications, Inc., and ValueClick, Inc.

## Edgar Filing: HARTE HANKS INC - Form 10-K

The S&P Index includes 500 United States companies in the industrial, transportation, utilities and financial sectors and is weighted by market capitalization. The peer groups are also weighted by market capitalization.

The graph depicts the results of investing \$100 in our common stock, the S&P 500 Index and the peer groups at closing prices on December 31, 2007 and assumes the reinvestment of dividends.

Table of Contents

	<b>Base Period Dec-07</b>	<b>Dec-08</b>	<b>Dec-09</b>	<b>Years Ending Dec-10</b>	<b>Dec-11</b>	<b>Dec-12</b>
Harte-Hanks, Inc.	100	37.13	66.40	80.57	59.35	40.99
S&P 500 Index	100	63.00	79.67	91.68	93.61	108.59
Peer Group	100	61.34	88.17	113.17	112.05	132.78

Table of Contents**ITEM 6. SELECTED FINANCIAL DATA**

The following table sets forth our summary historical financial information for the periods ended and as of the dates indicated. You should read the following historical financial information along with Management's Discussion and Analysis of Financial Condition and Results of Operations contained in this Form 10-K. The fiscal year financial information included in the table below for the years ended December 31, 2012, 2011, and 2010 is derived from audited financial statements contained in this Form 10-K. Information for the years ended December 31, 2009 and 2008 was derived from previously filed Annual Reports on Form 10-K. All financial information presented below excludes amounts related to our Florida Shoppers operations, which were sold on December 31, 2012.

In thousands, except per share amounts	2012	2011	2010	2009	2008
<b>Statement of Comprehensive Income Data</b>					
Revenues	\$ 767,709	\$ 811,636	\$ 820,720	\$ 817,104	\$ 1,021,596
<b>Operating expenses</b>					
Labor, production and distribution	615,527	649,340	641,662	635,067	789,720
Advertising, selling, general and administrative	64,765	65,607	64,079	58,813	76,717
Impairment of goodwill	156,936	0	0	0	0
Shoppers legal settlement	0	(1,260)	0	6,950	0
Depreciation and software amortization	20,176	19,622	21,443	26,203	31,476
Intangible amortization	245	229	290	716	1,903
Total operating expenses	857,649	733,538	727,474	727,749	899,816
Operating income (loss)	(89,940)	78,098	93,246	89,355	121,780
Interest expense, net	3,483	2,935	2,624	7,968	13,823
Income (loss) from continuing operations	\$ (73,104)	\$ 45,877	\$ 55,194	\$ 50,963	\$ 64,276
Earnings (loss) from continuing operations per common share diluted	\$ (1.16)	\$ 0.72	\$ 0.86	\$ 0.80	\$ 1.00
Weighted-average common and common equivalent shares outstanding diluted	62,887	63,552	64,139	63,885	64,104
<b>Segment Data</b>					
<b>Revenues</b>					
Direct Marketing	\$ 581,091	\$ 614,270	\$ 601,283	\$ 585,988	\$ 732,740
Shoppers	186,618	197,366	219,437	231,116	288,856
Total revenues	\$ 767,709	\$ 811,636	\$ 820,720	\$ 817,104	\$ 1,021,596
<b>Operating income (loss)</b>					
Direct Marketing	\$ 75,398	\$ 83,490	\$ 86,748	\$ 95,812	\$ 103,121
Shoppers	(152,610)	5,839	17,795	5,571	30,347
General corporate	(12,728)	(11,231)	(11,297)	(12,028)	(11,688)
Total operating income (loss)	\$ (89,940)	\$ 78,098	\$ 93,246	\$ 89,355	\$ 121,780
<b>Other Data</b>					
Cash dividends per share	\$ 0.43	\$ 0.32	\$ 0.30	\$ 0.30	\$ 0.30
Capital expenditures	\$ 13,856	\$ 20,970	\$ 17,201	\$ 8,828	\$ 19,506
<b>Balance sheet data (at end of period)</b>					
Current assets	\$ 225,500	\$ 271,638	\$ 264,959	\$ 253,174	\$ 235,307
Property, plant and equipment, net	61,971	68,892	69,275	74,260	91,428
Goodwill and other intangibles, net	413,974	571,155	571,384	558,409	559,116
Total assets	706,212	916,325	909,804	889,689	889,747
Total debt	110,250	179,438	193,000	239,688	270,625
Total stockholders' equity	\$ 328,164	\$ 446,355	\$ 437,823	\$ 401,643	\$ 356,372

Table of Contents

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**Cautionary Note About 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 the cautionary note included under Item 1A above, which is provided pursuant to the safe harbor provisions of Section 27A of the 1933 Act and Section 21E of the 1934 Act. Actual results may vary materially from what is expressed in or indicated by the forward-looking statements.

**Overview**

The following MD&A section is intended to help the reader understand the results of operations and financial condition of Harte-Hanks, Inc. (Harte-Hanks). 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.

Harte-Hanks is a worldwide direct and targeted marketing company that provides multichannel direct and digital marketing services and shopper advertising opportunities to a wide range of local, regional, national and international consumer and business-to-business marketers. We manage our operations through two operating segments: Direct Marketing and Shoppers.

Our Direct Marketing services offer a wide variety of integrated, multichannel, 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 multichannel 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 and data management software, in media from direct mail to email, including:

- agency and digital services;
- database marketing solutions;
- data quality software and services with Trillium Software;
- business-to-business lead generation;

## Edgar Filing: HARTE HANKS INC - Form 10-K

- direct mail and fulfillment; and
- contact centers.

In 2012, our Direct Marketing segment had revenues of \$581.1 million, which represented 76% of our total revenues.

Harte-Hanks Shoppers is North America's largest owner, operator and distributor of shopper publications, based on weekly circulation and revenues. Shoppers are weekly advertising publications, 7 by 10 inches in size, distributed free by Standard Mail to households and businesses in a particular geographic area. Through print and digital offerings, Shoppers is a trusted local source for saving customers money and helping businesses grow. Shoppers offer advertisers a geographically targeted, cost-effective local advertising system, with virtually 100% penetration in their area of distribution. Shoppers are particularly effective in large markets with high media fragmentation in which major metropolitan newspapers generally have low penetration. Our Shoppers segment also provides online advertising and other services through our website, *PennySaverUSA.com*®, as well as business websites and search engine marketing. Our websites are online advertising portals, bringing buyers and sellers together through our online offerings, such as local classifieds, business listings, coupons, special offers and PowerSites. PowerSites are templated websites for our customers, optimized to help small and medium-sized business owners establish a web presence and improve their lead generation. At December 31, 2011, we were publishing approximately 5,600 PowerSites weekly.

## Edgar Filing: HARTE HANKS INC - Form 10-K

### Table of Contents

On December 31, 2012 we sold the assets of our Florida Shoppers operations, The Flyer®, for gross proceeds of \$2.0 million, subject to working capital adjustments. This transaction resulted in an after-tax loss of \$2.7 million. Because the Florida Shoppers represent a distinct business unit with operations and cash flows that can clearly be distinguished, both operationally and for financial purposes, from the rest of Harte-Hanks, Inc., the results of the Florida Shoppers operations are reported as discontinued operations for all periods presented. Results of the remaining Harte-Hanks, Inc. business segments are reported as continuing operations.

After this sale, Harte-Hanks Shoppers no longer has any operations or circulation in the state of Florida. All of our Shopper operations are now located in California, and our California publications now account for all of Shoppers weekly circulation. As of December 31, 2012, Shoppers delivered approximately 9.1 million shopper packages in six major markets each week, covering Southern, Central and Northern California.

In 2012, our Shoppers segment, excluding the Florida Shoppers, had revenues of \$186.6 million, which represented 24% of our total revenues.

We derive revenues from the sale of direct marketing services and shopper advertising services.

As a worldwide business, Direct Marketing is affected by general national and international economic and business conditions. Marketing budgets are often more discretionary in nature, and are easier to reduce in the short-term than other expenses in response to weak economic conditions. Direct Marketing 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.

Prior to the sale of our Florida Shoppers in 2012, our Shoppers business operated in regional markets in both California and Florida and was greatly affected by the strength of the state and local economies. Revenues from our Shoppers business were largely dependent on local advertising expenditures in the areas of California and Florida in which we operated. During 2012, the poor economic conditions that we have experienced since the second half of 2007 in California and Florida continued. These conditions were initially created by weakness in the real estate and associated financing markets and have spread and persist across virtually all categories. As a result of management's evaluation of the Shoppers business, we recorded a \$165.3 million impairment loss in the second quarter of 2012 related to Shoppers' goodwill and other intangible assets. Excluding the Florida Shoppers operations, the total impairment charge related to our Shoppers business was \$156.9 million. We see some improvement in the California economy, but we expect to have further challenges before our performance improves. In response, during 2012, we continued our efforts to reduce expenses in the Shoppers business, primarily through organizational restructuring, and the discontinuance of a number of unprofitable digital initiatives, including SaverTime and mobile apps. We also made plans to close our production facility in Northern California in 2013. We continue to invest in online offerings, particularly our PowerSites, where we are seeing good revenue growth and are adding capabilities that provide value for our readers and advertisers, and in other profitable digital initiatives. We believe the steps we are taking to improve overall efficiency, combined with our continued investments in digital initiatives, will improve our Shoppers performance in the long term.

Our principal operating expense items are labor, postage and transportation.





Table of Contents**Results of Continuing Operations**

As discussed in Note P, *Discontinued Operations*, we sold the assets of our Florida Shoppers operations on December 31, 2012. Therefore, the operating results of our Florida Shoppers, including the loss on the sale, are being reported as discontinued operations in the Consolidated Financial Statements, and are excluded from management's discussion and analysis of financial condition and results of operations below.

Operating results from continuing operations, direct marketing and California shoppers, were as follows:

<b>In thousands except per share amounts</b>	<b>2012</b>	<b>% Change</b>	<b>2011</b>	<b>% Change</b>	<b>2010</b>
Revenues	\$ 767,709	-5.4	\$ 811,636	-1.1	\$ 820,720
Operating expenses	857,649	16.9	733,538	0.8	727,474
Operating income (loss)	\$ (89,940)	-215.2	\$ 78,098	-16.2	\$ 93,246
Income (loss) from continuing operations	\$ (73,104)	-259.3	\$ 45,877	-16.9	\$ 55,194
Diluted EPS from continuing operations	\$ (1.16)	-261.1	\$ 0.72	-16.3	\$ 0.86

Year ended December 31, 2012 vs. Year ended December 31, 2011*Revenues*

Consolidated revenues decreased \$43.9 million, to \$767.7 million, in 2012 compared to 2011. Our overall results reflect decreased revenues of \$33.2 million, or 5.4%, from our Direct Marketing segment and decreased revenues of \$10.7 million, or 5.4%, from our Shoppers segment. Direct Marketing results reflect the impact of a large, long standing retail customer which changed its marketing strategy to emphasize broadcast at the expense of direct mail. Direct Marketing experienced decreased revenues from all of our verticals, with the high-tech vertical representing the largest dollar decrease. Shoppers' revenue performance reflects the continued impact that the difficult economic environment in California is having on our Shoppers business. The decrease in revenues was the result of decreased sales in established markets, including declines from most revenue categories. Revenues from in-book advertising decreased at a higher rate than revenues from distribution products. Shoppers revenues increased from the automotive, consumer spending and communications sectors, and decreased from the services and real estate sectors.

*Operating Expenses*

Overall operating expenses were \$857.6 million in 2012, compared to \$733.5 million in 2011. This \$124.1 million increase was a result of the impairment charge of \$156.9 million discussed above. Excluding this impairment charge, operating expenses decreased \$32.8 million, or 4.5%,

## Edgar Filing: HARTE HANKS INC - Form 10-K

compared to 2011. This \$32.8 million decrease in operating expenses was driven by decreased operating expenses in Direct Marketing of \$25.1 million, or 4.7%, and decreased operating expenses of \$9.2 million, or 4.8%, in Shoppers, partially offset by an increase in general corporate expense of \$1.5 million, or 13.3%. The decrease at Direct Marketing was primarily due to decreased outsourced costs resulting from decreased outsourced volumes, decreased mail supply chain costs resulting from decreased volumes, and reductions in headcount, temporary labor, incentive compensation and commissions, all as a result of revenue performance. The decrease at Shoppers was due to decreased severance costs, decreased stock-based compensation, lower payroll costs due to lower ad sales and headcount reductions, decreases in newsprint and job paper expenses due to declines in volumes, decreased bad debt expense and decreased facility lease expense. The overall decrease at Shoppers was partially offset by costs accrued for the closure of the Northern California production facility, legal accrual reductions in 2011, an increase in offload printing costs due to an increase in heatset volumes, an increase in postage costs due to the January 2012 postage rate increase, an increase in outsourced costs due to increased outsourced volumes, and the write-off of software related to various digital initiatives. The increase in general corporate expense was attributable to increased pension expense resulting from using a lower discount rate to calculate the projected pension benefit obligation.

Table of Contents

*Income/Earnings Per Share from Continuing Operations*

We recorded a loss from continuing operations of \$73.1 million, and diluted loss per share from continuing operations of \$1.16, in 2012. Excluding the impairment loss, income from continuing operations and diluted earnings per share from continuing operations for 2012 would have been \$39.0 million and \$0.62, respectively. These results, excluding the impairment loss, compare to income from continuing operations of \$45.9 million, and diluted earnings per share from continuing operations of \$0.72 in 2011. The decrease in income from continuing operations, excluding the impairment loss, is primarily a result of decreased operating income from both Direct Marketing and Shoppers, a gain on the sale of land in 2011, changes in net foreign currency transaction gains and losses, and an increase in general corporate expense.

Year ended December 31, 2011 vs. Year ended December 31, 2010

*Revenues*

Consolidated revenues decreased \$9.1 million, to \$811.6 million, in 2011 compared to 2010. Our overall results reflect increased revenues of \$13.0 million, or 2.2%, from our Direct Marketing segment and decreased revenues of \$22.1 million, or 10.1%, from our Shoppers segment. The Direct Marketing results were affected by a large, one-time, voluntary recall project performed for a long-time pharmaceutical customer during the second half of 2010. Excluding the results from this project, total Direct Marketing revenues increased \$29.1 million, or 5.0% in 2011 compared to 2010. Direct Marketing experienced increased revenues from our select, retail and financial verticals, which were partially offset by decreased revenues from our healthcare and high-tech vertical. The August 2010 acquisition of Information Arts also contributed to the 2011 revenue growth. Shoppers revenue performance reflects the continued impact that the difficult economic environment in California is having on our Shoppers business. The decrease in revenues was the result of decreased sales in established markets, including declines in most revenue categories.

*Operating Expenses*

Overall operating expenses increased 0.8%, to \$733.5 million, in 2011 compared to 2010. The overall increase in operating expenses was driven by increased operating expenses in Direct Marketing of \$16.2 million, or 3.2%. The Direct Marketing increase was primarily due to increased headcount to support revenues and improve our database service capabilities, higher mail supply chain costs on higher transportation volumes, increased travel and increased employee recruiting. The acquisition of Information Arts also contributed to the increase in Direct Marketing operating expenses. Shoppers operating expenses decreased \$10.1 million, or 5.0%, due to lower variable payroll costs, decreased postage due to lower distribution volumes and the elimination of the second day edition, decreased outsourced costs on lower volumes, decreased lease expense due to facility consolidations, and a \$1.3 million reduction of a legal accrual. The overall decrease at Shoppers was partially offset by \$4.1 million of charges recognized in the first half of 2011 related to our efforts to reduce expenses in the Shoppers business. Of these charges, \$3.9 million related to the retirement of the President of our Shoppers business and severance due to headcount reductions. The remaining charges related to facilities and other miscellaneous items. The decrease at Shoppers was also partially offset by an increase in newsprint expense due to higher paper rates. Excluding the retirement, severance and other charges, and the legal accrual reduction, Shoppers operating expenses decreased \$12.9 million, or 6.4%.

*Income/Earnings Per Share from Continuing Operations*

## Edgar Filing: HARTE HANKS INC - Form 10-K

Income from continuing operations decreased 16.9%, to \$45.9 million, and diluted earnings per share from continuing operations decreased 16.3%, to \$0.72 per share, in 2011 compared to 2010. These decreases were the result of decreased operating income from both Shoppers and Direct Marketing, higher interest expense, and a higher effective tax rate in 2011 compared to 2010. These decreases were partially offset by a \$2.3 million gain on the sale of land adjacent to our Shopper s Brea facility, and a \$1.3 million change in net foreign currency transaction gains and losses.

Table of Contents**Direct Marketing**

Direct Marketing operating results were as follows:

<b>In thousands</b>	<b>2012</b>	<b>% Change</b>	<b>2011</b>	<b>% Change</b>	<b>2010</b>
Revenues	\$ 581,091	-5.4	\$ 614,270	2.2	\$ 601,283
Operating expenses	505,693	-4.7	530,780	3.2	514,535
Operating income	\$ 75,398	-9.7	\$ 83,490	-3.8	\$ 86,748

Year ended December 31, 2012 vs. Year ended December 31, 2011*Revenues*

Direct Marketing revenues decreased \$33.2 million, or 5.4%, in 2012 compared to 2011. These results reflect the impact of a large, long standing retail customer which changed its marketing strategy to emphasize broadcast at the expense of direct mail. Despite the shift in strategy and reduced direct mail volumes, this company remains one of our largest customers. Reduced revenues from this customer represented a little less than half of the overall decline in Direct Marketing revenues. Revenues from our retail vertical declined 1% compared to the prior year as increased spending by other existing retail customers somewhat offset the reduced spending by this customer. Revenues from our pharmaceutical vertical decreased 16% compared to 2012, reflecting the effect of volume reductions from one long standing customer beginning in the second quarter of 2012, and the loss of another long standing customer in the third quarter of 2012. Our high-tech vertical declined 9%, representing the largest dollar decrease from the prior year. Our select vertical declined 4% and our financial vertical declined 3%.

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, 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.

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

*Operating Expenses*

Operating expenses decreased \$25.1 million, or 4.7%, in 2012 compared to 2011. Labor costs decreased \$7.0 million, or 2.5%, primarily due to reductions in headcount and temporary labor, decreased incentive compensation and decreased commissions, all as a result of revenue performance. Production and distribution costs decreased \$19.5 million, or 10.2%, due to decreased outsourced costs resulting from decreased outsourced volumes, decreased mail supply chain costs resulting from decreased volumes, and decreased lease costs due to costs recognized in

## Edgar Filing: HARTE HANKS INC - Form 10-K

2011 to terminate a lease. General and administrative expense increased \$0.9 million, or 2.0%, due primarily to an increase in legal fees, increased royalties and increased employee travel and training, partially offset by decreased promotion expense and facilities costs. Depreciation and software amortization expense increased \$0.5 million, or 3.1%, due to increased capital expenditures in 2011. Intangible asset amortization was up slightly.

Direct Marketing'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 direct marketing 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 Direct Marketing's total production costs and total operating expenses, and may have an impact on future demand for our supply chain management.

Table of Contents

Year ended December 31, 2011 vs. Year ended December 31, 2010

*Revenues*

Direct Marketing revenues increased \$13.0 million, or 2.2%, in 2011 compared to 2010. These results were affected by a large, one-time, voluntary recall project performed for a long-time pharmaceutical customer during the second half of 2010. Excluding the results from this project, total Direct Marketing revenues increased \$29.1 million, or 5.0%, in 2011 compared to 2010. Revenues from our select vertical increased 17%, representing the largest dollar increase from the prior year. Our retail vertical increased 9% and our financial vertical increased 4%. Revenues from our pharmaceutical vertical declined 18% due to the recall project discussed above, and our high-tech vertical declined 7%. 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. The August 2010 acquisition of Information Arts also contributed to the 2010 revenue growth.

*Operating Expenses*

Operating expenses increased \$16.2 million, or 3.2%, in 2011 compared to 2010. Labor costs increased \$9.3 million, or 3.5%, due to increased headcounts to support revenues and improve our database service capabilities. Production and distribution costs increased \$6.4 million, or 3.4%, due to higher mail supply chain costs on higher transportation volumes. General and administrative expense increased \$2.2 million, or 4.8%, due primarily to an increase in travel and employee recruiting. Depreciation and software amortization expense decreased \$1.6 million, or 9.5%, due to decreased capital expenditures over the last few years. Intangible asset amortization was down \$0.1 million, or 20.9%, due to certain intangible assets becoming fully amortized.

**Shoppers**

Shoppers operating results were as follows:

<b>In thousands</b>	<b>2012</b>	<b>% Change</b>	<b>2011</b>	<b>% Change</b>	<b>2010</b>
Revenues	\$ 186,618	-5.4	\$ 197,366	-10.1	\$ 219,437
Operating expenses	339,228	77.1	191,527	-5.0	201,642
Operating income (loss)	\$ (152,610)	-2,713.6	\$ 5,839	-67.2	\$ 17,795

Year ended December 31, 2012 vs. Year ended December 31, 2011

*Revenues*



## Edgar Filing: HARTE HANKS INC - Form 10-K

Shoppers revenues decreased \$10.7 million, or 5.4%, in 2012 compared to 2011. These results reflect the continued impact that the difficult economic environment in California is having on our Shoppers business. The decrease in revenues was the result of decreased sales in established markets, including declines from most revenue categories. Revenues from in-book advertising decreased at a higher rate than revenues from distribution products. Shoppers revenues increased from the automotive, consumer spending and communications sectors. Revenues from the services and real estate sectors decreased.

At December 31, 2012, our Shoppers circulation reached approximately 9.1 million addresses in California each week. While we have not made any significant changes to our circulation in the last several years, we continue to evaluate all of our circulation performance and may make circulation reductions in the future as part of our efforts to address the difficult economic conditions in California.

Future revenue performance will depend on, among other factors, the overall strength of the California economy, as well as how successful we are at maintaining and growing business with existing clients, and acquiring new clients.

Table of Contents

*Operating Expenses*

Shoppers operating expenses were \$339.2 million in 2012, compared to \$191.5 million in 2011. This \$147.7 million year over year increase was primarily a result of the \$156.9 million impairment loss recorded in the second quarter of 2012, as discussed above. This increase was also impacted by \$1.3 million of costs recognized in the fourth quarter of 2012 relating to the closure of our production facility in Northern California. Excluding the impairment loss and facility closure costs, operating expenses decreased \$10.5 million, or 5.5%, compared to 2011. Total labor costs decreased \$10.1 million, or 15.7%, due to decreased severance costs (partially offset by severance costs related to the facility closure), decreased stock-based compensation, and lower payroll costs from lower ad sales, headcount reductions and pay rate reductions. Total production costs were up \$1.6 million, or 1.4%, due to an increase in offload printing costs due to an increase in heatset volumes, an increase in postage costs resulting from the January 2012 postage rate increase, and an increase in outsourced costs due to increased outsourced volumes, partially offset by decreases in newsprint and job paper expenses due to declines in volumes, and a decrease in facility lease expense. Total general and administrative costs decreased \$0.8 million, or 6.0%, due to a decrease in bad debt expense, lower credit card processing fees and lower costs associated with digital products, partially offset by a portion of the closing costs discussed above and legal accrual reductions in 2011. Depreciation and software amortization expense increased \$0.1 million, or 2.0%, due to writing off software related to various digital initiatives in the second quarter of 2012.

Shoppers largest cost components are postage, labor, and paper. Shoppers labor costs are partially variable and tend to fluctuate with the number of zones, circulation, volumes and revenues. Standard postage rates have increased in recent years, most recently in April 2011, January 2012 and January 2013. Shoppers postage rates increased by less than 1.0% as a result of the April 2011 rate increase, increased by approximately 2.1% as a result of the January 2012 rate increase, and will increase by approximately 2.8% as a result of the January 2013 rate increase. The January 2013 postage rate increase, and any additional future changes in postage rates will affect Shoppers distribution costs. The U. S. Postal Service has also proposed various changes in its services to address its financial performance, such as delivery frequency and facility access. Recently, the USPS announced it would end household delivery on Saturdays starting in August 2013. At this point we do not believe the announced and proposed changes will have a material impact on our Shoppers business. Newsprint prices increased steadily over the last two years before leveling off in the second half of 2012. Newsprint prices are expected to continue to remain at the current rates throughout 2013. Any future changes in newsprint prices will affect Shoppers production costs. Shoppers Northern California production facility will be closed in the third quarter of 2013. This facility closure will reduce Shoppers overall operating costs in 2013, including reductions in most significant expense lines.

Year ended December 31, 2011 vs. Year ended December 31, 2010

*Revenues*

Shoppers revenues decreased \$22.1 million, or 10.1%, in 2011 compared to 2010. These results reflect the continued impact that the difficult economic environment in California is having on our Shoppers business. The decrease in revenues was the result of decreased sales in established markets, including declines in most revenue categories. At December 31, 2011, our Shoppers circulation reached approximately 9.1 million addresses in California each week.

*Operating Expenses*

## Edgar Filing: HARTE HANKS INC - Form 10-K

Operating expenses decreased \$10.1 million, or 5.0%, in 2011 compared to 2010. During the first half of 2011, we incurred \$4.1 million of charges through our efforts to reduce expenses in the Shoppers business, primarily through organizational restructuring and headcount reductions. Of these charges, \$3.9 million related to the retirement of the President of our Shoppers business and severance due to headcount reductions. The remaining charges related to facilities and other miscellaneous items. Total labor costs decreased \$3.0 million, or 4.5%, due to lower variable payroll costs from lower ad sales, headcount reductions and lower incentive compensation. Excluding the severance and retirement charges described above, total labor costs decreased \$6.9 million, or 10.3%. Total production costs decreased \$4.9 million, or 4.3%, due primarily to decreased postage costs as a result of a decline in distribution volumes and the elimination of the second day edition in Southern California, decreased outsourced costs resulting from decreased outsourced volumes, and decreased lease expense due to facility consolidations and eliminations. These decreases were partially offset by an increase in newsprint expense due to higher paper rates. Total general and administrative costs decreased \$2.0

Table of Contents

million, or 12.6%, due primarily to a \$1.3 million reduction of a legal accrual. Depreciation and software amortization expense decreased \$0.2 million, or 4.9%, due to decreased capital expenditures in the last few years. Excluding the retirement, severance and other charges, and the legal accrual reduction, Shoppers operating expenses decreased \$12.9 million, or 6.4%.

**General Corporate Expense**

Year ended December 31, 2012 vs. Year ended December 31, 2011

General corporate expense increased \$1.5 million, or 13.3%, in 2012 compared to 2011. This increase was attributable to increased pension expense resulting from an increase in the projected pension benefit obligation due to a lower discount rate.

Year ended December 31, 2011 vs. Year ended December 31, 2010

General corporate expense decreased \$0.1 million, or 0.6%, in 2011 compared to 2010. This decrease was the result of lower incentive compensation due to overall financial results.

**Interest Expense**

Year ended December 31, 2012 vs. Year ended December 31, 2011

Interest expense increased \$0.4 million, or 12.2%, in 2012 compared to 2011, due to a higher interest rate spread as a result of the 2011 Term Loan Facility, which replaced the 2006 Term Loan Facility in August 2011. This increase was partially offset by lower average debt balances in 2012 due to the maturity and \$60.0 million payoff of the 2008 Term Loan in March of 2012.

Year ended December 31, 2011 vs. Year ended December 31, 2010

Interest expense increased \$0.4 million, or 12.8%, in 2011 compared to 2010, due to a higher interest rate spread and an increased debt balance as a result of the 2011 Term Loan Facility, which replaced the 2006 Term Loan Facility in August 2011.

Our debt at December 31, 2012 and 2011 is described in Note D *Long-Term Debt* in the Notes to Consolidated Financial Statements.

**Interest Income**

Year ended December 31, 2012 vs. Year ended December 31, 2011

Interest income decreased \$0.2 million, or 63.5% in 2012 compared to 2011 due to lower average balances and lower returns on invested cash and cash equivalents in 2012.

Year ended December 31, 2011 vs. Year ended December 31, 2010

Interest income increased slightly in 2011 compared to 2010 due to higher returns on invested cash and cash equivalents in 2011.

**Other Income and Expense**

Year ended December 31, 2012 vs. Year ended December 31, 2011

Other expense, net, was \$2.9 million in 2012, a \$4.4 million change from other income, net of \$1.5 million in 2011. This change was primarily due to a \$2.3 million gain on the sale of land adjacent to our Shopper's Brea facility, and a \$2.2 million change in net foreign currency transaction gains and losses.

Year ended December 31, 2011 vs. Year ended December 31, 2010

Other income, net, was \$1.5 million in 2011, a \$3.6 million change from other net expense of \$2.1 million in 2010. This change was primarily due to a \$2.3 million gain on the sale of land adjacent to our Shopper's Brea facility, and a \$1.3 million change in net foreign currency transaction gains and losses.

Table of Contents

**Income Taxes**

Year ended December 31, 2012 vs. Year ended December 31, 2011

Our income tax benefit of \$23.2 million for 2012 resulted in an effective income tax rate of 24.1%. The income tax benefit for 2012 reflects the \$156.9 million impairment charge that resulted in a \$44.8 million tax benefit in the second quarter of 2012. In addition, the value of the net operating loss related to the Florida Shoppers operations at the beginning of 2012 is now attributed to continuing operations. Excluding the impairment charges and the deduction related to the Florida net operating loss, 2012 tax expense would have been \$23.0 million with an effective tax rate of 37.9%. This compares to an income tax expense of \$30.8 million and an effective tax rate 40.2% for 2011.

Year ended December 31, 2011 vs. Year ended December 31, 2010

Income taxes decreased \$2.5 million in 2011 compared to 2010 due to lower pretax income levels, partially offset by a higher effective tax rate. The effective income tax rate for 2011 was 40.2% compared to 37.6% in 2010. The increase in the effective tax rate is primarily due to a reduction to our uncertain tax liabilities related to state income taxes in 2010.

**Economic Climate and Impact on our Financial Statements**

The economic climate in California and Florida had a negative impact on our Shoppers operations and cash flows for the year ended December 31, 2012, and our financial position at December 31, 2012. This impact is reflected in our financial results, including the \$165.3 million impairment charge related to goodwill and other intangible assets recorded in the second quarter of 2012. Excluding the Florida Shoppers operations, which were sold at the end of 2012 and are reported as discontinued operations, the total impairment charge related to our Shoppers business was \$156.9 million. We cannot predict the duration of the current difficult economic environment in California, or the timing or magnitude of any subsequent improvement. If the economic climate and markets we serve fail to improve (or deteriorate), we may record additional charges, including charges related to restructuring costs and the impairment of goodwill, other intangibles and long-lived assets, and our operations, cash flows and financial position may be materially and adversely affected.

**Liquidity and Capital Resources**

**Sources and Uses of Cash**

As of December 31, 2012, cash and cash equivalents were \$49.6 million, decreasing \$37.1 million from cash and cash equivalents at December 31, 2011. This net decrease was a result of net cash provided by operating activities of \$76.3 million, offset by net cash used in investing activities of \$13.8 million and net cash used in financing activities of \$99.8 million.

## Operating Activities

Net cash provided by operating activities in 2012 was \$76.3 million, compared to \$60.7 million in 2011. The \$15.6 million year-over-year increase was attributable to the changes within working capital assets and liabilities.

In 2012, our principal working capital changes, which directly affected net cash provided by operating activities, were as follows:

- A decrease in accounts receivable attributable to collection of the December 31, 2011 receivables as well as higher revenues in the fourth quarter of 2011 compared to the fourth quarter of 2012. Days sales outstanding were approximately 64 days at December 31, 2012, which decreased from 66 days at December 31, 2011;
- A decrease in inventory due to purchasing and holding higher levels of newsprint inventory in prior periods in advance of increases in newsprint prices;
- An increase in prepaid expenses and other current assets due to timing of payments;

Table of Contents

- A decrease in accounts payable due to lower overall production and distribution expense in the fourth quarter of 2011 than in the fourth quarter of 2012;
- A decrease in accrued payroll and related expenses due to the payment of 2011 incentive compensation and lower accrued incentive compensation at December 31, 2012 than at December 31, 2011;
- An increase in deferred revenue and customer advances due to timing of receipts;
- An increase in customer postage and program deposits due to the timing of a new customer rebate program; and
- A decrease in income taxes payable due to overpayment of estimated taxes payments in 2012. The overpayment was the result of the loss on the sale of Florida Shoppers operations at the end of 2012.

**Investing Activities**

Net cash used in investing activities was \$13.8 million in 2012, compared to \$17.6 million in 2011. The \$3.7 million decrease is primarily the result of a \$7.1 million decrease in capital spending in 2012 compared to 2011, partially offset by \$3.4 million received in connection with the sale of land in 2011.

**Financing Activities**

Net cash used in financing activities was \$99.8 million in 2012 compared to \$42.2 million in 2011. The \$57.7 million increase is attributable to \$55.6 million in higher net debt repayments in 2012 than in 2011 due to the five-year \$122.5 million term loan facility obtained in August 2011. The additional dividend in the fourth quarter of 2012 also contributed to this increase. This increase was partially offset by a \$4.0 million decrease in treasury stock purchases in 2012 compared to 2011.

**Credit Facilities**

On March 7, 2008, we entered into a four-year \$100 million term loan facility (2008 Term Loan Facility) with Wells Fargo Bank, N.A., as Administrative Agent. The 2008 Term Loan Facility matured on March 7, 2012, at which time we paid the remaining outstanding principal of \$60.0 million using cash on hand.

On August 12, 2010, we entered into a new three-year \$70 million revolving credit facility, which includes a \$25 million accordion feature, a \$25 million letter of credit sub-facility and a \$5 million swing line loan sub-facility (2010 Revolving Credit Facility), with Bank of America, N.A., as Administrative Agent. The 2010 Revolving Credit Facility permits us to request up to a \$25 million increase in the total amount of the facility. The 2010 Revolving Credit Facility matures on August 12, 2013. For each borrowing under the 2010 Revolving Credit Facility, we can generally choose to have the interest rate for that borrowing calculated on either (i) the LIBOR rate (as defined in the 2010 Revolving Credit



## Edgar Filing: HARTE HANKS INC - Form 10-K

Facility) for the applicable interest period, plus a spread which is determined based on our total net debt-to-EBITDA ratio (as defined in the 2010 Revolving Credit Facility) then in effect, which ranges from 2.25% to 3.00% per annum; or (ii) the highest of (a) the Federal Funds Rate plus 0.50%, (b) the Agent's prime rate, and (c) the LIBOR rate plus 1.00%, plus a spread which is determined based on our total net debt-to-EBITDA ratio then in effect, which ranges from 1.25% to 2.00% per annum. There is a facility fee that we are also required to pay under the 2010 Revolving Credit Facility. The facility fee rate ranges from 0.40% to 0.45% per annum, depending on our total net debt-to-EBITDA ratio then in effect. In addition, there is 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 LIBOR 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 any amounts drawn on the 2010 Revolving Credit Facility at any time. At December 31, 2012, we did not have any outstanding amounts drawn against our 2010 Revolving Credit Facility. At December 31, 2012, we had letters of credit totaling \$9.5 million issued under the 2010 Revolving Credit Facility, decreasing the amount available for borrowing to \$60.5 million.

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

# Edgar Filing: HARTE HANKS INC - Form 10-K

## Table of Contents

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 December 31, 2012, we had \$110.3 million outstanding under the 2011 Term Loan Facility.

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 3.0 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 20% of the consolidated revenue, assets or EBITDA 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 December 31, 2012, we were in compliance with all of the covenants of our credit facilities.

## **Contractual Obligations**

Contractual obligations at December 31, 2012 are as follows:

<b>In thousands,</b>	<b>Total</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>Thereafter</b>
Debt	\$ 110,250	\$ 12,250	\$ 15,313	\$ 18,375	\$ 64,312	\$ 0	\$ 0

Edgar Filing: HARTE HANKS INC - Form 10-K

Interest on debt (1)	7,005	2,369	2,085	1,699	852	0	0
Operating leases	49,273	15,689	12,762	7,884	5,510	3,937	3,491
Capital leases	671	369	212	73	16	1	0
Deferred compensation liability	2,830	702	702	352	0	0	1,074
Unfunded pension plan benefit payments	28,211	1,437	1,431	1,425	1,418	1,449	21,051
Other long-term obligations	194	122	55	17	0	0	0
Total contractual cash obligations	\$ 198,434	\$ 32,938	\$ 32,560	\$ 29,825	\$ 72,108	\$ 5,387	\$ 25,616

(1) Future interest amounts were estimated using the December 31, 2012 effective rate on our outstanding debt of 2.21%.

At December 31, 2012, we had total letters of credit in the amount of \$9.9 million. No amounts were drawn against these letters of credit at December 31, 2012. These letters of credit renew annually and exist to support insurance programs relating to workers' compensation, automobile and general liability. We had no other off-balance sheet arrangements at December 31, 2012.

Table of Contents

**Dividends**

We paid a quarterly dividend of 8.5 cents per share in each of the first three quarters of 2012 and two dividends of 8.5 cents per share in the fourth quarter of 2012. The second dividend paid in the fourth quarter of 2012 was a one-time acceleration of the regular quarterly dividend we would have paid in the first quarter of 2013. As a result, we do not anticipate paying a dividend in the first quarter of 2013. We currently plan to pay a quarterly dividend of 8.5 cents per share in each of the second, third and fourth quarters of 2013, although any actual dividend declaration can be made only upon approval of our Board of Directors, based on its business judgment. We have paid consecutive quarterly dividends since the first quarter of 1995.

**Share Repurchase**

During 2012, we repurchased 0.7 million shares of our common stock for \$4.4 million under our stock repurchase program that was publicly announced in August 2012. Under this program our Board of Directors has authorized us to spend up to \$10.0 million to repurchase shares of our outstanding common stock. At December 31, 2012, we had authorization to spend \$5.6 million to repurchase additional shares under this program. From 1997 through December 2012, we have supported our stockholders by spending more than \$1.2 billion to repurchase 65.6 million shares under this program and previously announced programs.

**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 2010 Revolving Credit Facility, subject to the terms and conditions of that facility.

The amount of cash on hand and borrowings available under our 2010 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 December 31, 2012, we had \$60.5 million of unused borrowing capacity under our 2010 Revolving Credit Facility (which matures on August 12, 2013) and a cash balance of \$49.6 million. Based on our current operational plans, we believe that our cash on hand, cash provided by operating activities, and availability under the 2010 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 United States and other economies could have a material adverse effect on our business, financial position or operating results.

## Edgar Filing: HARTE HANKS INC - Form 10-K

Our 2010 Revolving Credit Facility matures in August 2013. We believe that we will be able to obtain a replacement revolver facility in a similar amount and with similar terms. However, if there are disruptions in the credit markets, we may be unable to obtain a replacement facility on acceptable terms or at all. In that event, depending on our ability to generate sufficient cash flow from operations, our overall liquidity and ability to make payments on our indebtedness under our 2011 Term Loan Facility (which matures in August 2016) may be adversely impacted, and we may be required to seek one or more alternatives, such as refinancing or restructuring our indebtedness, selling material assets or operations, or seeking to raise debt or equity capital. We cannot assure you that any of these actions could be affected on a timely basis or on satisfactory terms, if at all. In addition, our existing debt agreements contain restrictive covenants that may prohibit us from adopting one or more of these alternatives.

Table of Contents

**Critical Accounting Policies**

Critical accounting policies are defined as those that, in our judgment, are most important to the portrayal of our company's financial condition and results of operations and which require complex or subjective judgments or estimates. The areas that we believe involve the most significant management estimates and assumptions are detailed below. Actual results could differ materially from those estimates under different assumptions and conditions. Historically, actual results have not differed significantly from our estimates.

**Revenue Recognition**

We recognize revenue when all of the following criteria are satisfied: (i) persuasive evidence of an arrangement exists; (ii) the price is fixed or determinable; (iii) collectability is reasonably assured; and (iv) the service has been performed or the product has been delivered.

Payments received in advance of the performance of services or delivery of the product are recorded as deferred revenue until such time as the services are performed or the product is delivered.

Our accounting policy for revenue recognition has an impact on our reported results and relies on certain estimates that require judgments on the part of management. The portion of our revenue that is most subject to estimates and judgments is revenue recognized using the proportional performance method, as discussed below.

Direct Marketing revenue is derived from a variety of services and products, and may be billed at hourly rates, monthly rates or a fixed price. For all sales, we require either a purchase order, a statement of work signed by the client, a written contract, or some other form of written authorization from the client.

Revenue from agency and creative services, analytical services and market research is typically billed based on time and materials or at a fixed price. If billed at a fixed price, revenue is recognized on a proportional performance basis as the services specified in the arrangement are performed. In most cases, proportional performance is based on the ratio of direct costs incurred to total estimated costs where the costs incurred, primarily labor hours and outsourced services, represent a reasonable surrogate for output measures or contract performance. For fixed fee market research revenue streams, revenue is recognized in proportion to the value of service provided based on output criteria.

Revenue from email marketing, social media marketing and other digital solutions is recognized as the work is performed. Revenue from these services is typically based on a fixed price or rate given to the client.

Revenue associated with new marketing database builds is deferred until complete or until client acceptance. Upon completion or acceptance, revenue and direct build costs are then recognized over the term of the related arrangement as the services are provided. Revenue from database

## Edgar Filing: HARTE HANKS INC - Form 10-K

and website hosting services is recognized ratably over the contractual hosting period. Pricing for database builds are typically based on a fixed price and hosting fees are typically based on a fixed price per month or per contract.

Revenue from technology database subscriptions is based on a fixed price and is recognized ratably over the term of the subscription. Revenue from stand-alone technology data sales is recognized at the time of delivery.

Revenue from services such as data processing, printing, personalization of communication pieces using laser and inkjet printing, targeted mail, and transportation logistics is recognized as the work is performed. Revenue from these services is typically based on a fixed price or rate given to the client. Postage costs of mailings in our direct mail business are borne by our clients and are not directly reflected in our revenues or expenses.

Revenue related to fulfillment and contact centers, including inbound and outbound calling and email management, is also typically based on a fixed price per transaction or service provided. Revenue from these services is recognized as the service or activity is performed.

Table of Contents

Revenue from software arrangements involving multiple elements is allocated to each element based on the vendor-specific objective evidence of fair values of the respective elements. For software sales with multiple elements (for example, software licenses with undelivered post-contract customer support or PCS ), we allocate revenue to each component of the arrangement using the residual value method based on the fair value of the undelivered elements. This means we defer revenue from the software sale equal to the fair value of the undelivered elements. The fair value of PCS is based upon separate sales of renewals to other clients. The fair value of services, such as training and consulting, is based upon separate sales of these services to other clients.

The revenue allocated to PCS is recognized ratably over the term of the support period. Revenue allocated to professional services is recognized as the services are performed. The revenue allocated to software products, including time-based software licenses, is recognized, if collection is probable, upon execution of a licensing agreement and shipment of the software or ratably over the term of the license, depending on the structure and terms of the arrangement. If the licensing agreement is for a term of one year or less and includes PCS, we recognize the software and the PCS revenue ratably over the term of the license.

For certain non-software arrangements, we enter into contracts that include delivery of a combination of two or more of our service offerings. Such arrangements are divided into separate units of accounting, provided that the delivered element(s) has stand-alone value and objective and reliable evidence of the fair value of the undelivered element(s) exist(s).

When we are able to unbundle the arrangement into separate units of accounting, revenue from each service is recognized separately, and in accordance with our revenue recognition policy for each element. If we are unable to unbundle the arrangement into separate units of accounting, we apply one of the revenue recognition policies to the entire arrangement. This might impact the timing of revenue recognition, but would not change the total revenue recognized from the arrangement.

Shopper services are considered rendered, and the revenue recognized, when all printing, sorting, labeling and ancillary services have been provided and the mailing material has been received by the USPS.

Taxes collected from customers and remitted to governmental authorities are not reflected in our revenues or expenses.

**Allowance for Doubtful Accounts**

We maintain our allowance for doubtful accounts at a balance adequate to reduce accounts receivable to the amount of cash expected to be realized upon collection. The methodology used to determine the minimum allowance balance is based on our prior collection experience and is generally related to the accounts receivable balance in various aging categories. The balance is also influenced by specific clients' financial strength and circumstance. Accounts that are determined to be uncollectible are written off in the period in which they are determined to be uncollectible. Periodic changes to the allowance balance are recorded as increases or decreases to bad debt expense, which is included in the Advertising, selling, general and administrative line of our Consolidated Statements of Comprehensive Income (Loss). We recorded bad debt expense of \$1.1 million, \$1.4 million and \$1.6 million for the years ended December 31, 2012, 2011 and 2010, respectively. At December 31, 2012 and 2011, our allowance for doubtful accounts was \$3.4 million and \$3.2 million, respectively. While we believe our reserve estimate to be appropriate, we may find it necessary to adjust the allowance for doubtful accounts if future bad debt expense exceeds the estimated reserve. Given the significance of accounts receivable to the consolidated financial statements, the determination of net realizable values is considered to



be a critical accounting estimate.

**Reserve for Healthcare, Workers Compensation, Automobile and General Liability**

We are self-insured for our workers compensation, automobile, general liability and a portion of our healthcare insurance. We make various subjective judgments about a number of factors in determining our reserve for healthcare, workers compensation, automobile and general liability insurance, and the related expense. Our

Table of Contents

deductible for individual healthcare claims is \$0.3 million. Our deductible for workers' compensation is \$0.5 million. We have a \$0.3 million deductible for automobile and general liability claims. Our insurance administrator provides us with estimated loss reserves, based upon its experience dealing with similar types of claims, as well as amounts paid to date against these claims. We apply actuarial factors to both insurance estimated loss reserves and to paid claims and then determine reserve levels, taking into account these calculations. At December 31, 2012 and 2011, our reserve for healthcare, workers' compensation, automobile and general liability was \$11.4 million and \$12.1 million, respectively. If ultimate losses were 10% higher than our estimate at December 31, 2012, net income would be impacted by approximately \$0.7 million, net of taxes. The amount that earnings would be impacted is dependent on the claim year and our deductible levels for that plan year. Periodic changes to the reserve for workers' compensation, automobile and general liability are recorded as increases or decreases to insurance expense, which is included in the Advertising, selling, general and administrative line of our Consolidated Statements of Comprehensive Income (Loss). Periodic changes to the reserve for healthcare are recorded as increases or decreases to employee benefits expense, which is included in the Labor line of our Consolidated Statements of Comprehensive Income (Loss).

**Goodwill**

Goodwill is recorded to the extent that the purchase price of an acquisition exceeds the fair value of the identifiable net assets acquired. We assess the impairment of our goodwill by determining the fair value of each of our reporting units and comparing the fair value to the carrying value for each reporting unit. Determining fair value requires the exercise of significant judgments, including judgments about appropriate discount rates, the amount and timing of expected future cash flows, and perpetual growth rates. We have identified our reporting units as Direct Marketing and Shoppers. At December 31, 2012 and 2011, the net book value of our goodwill was allocated to our reporting units as follows:

In thousands	December 31,	
	2012	2011
Direct Marketing	\$ 398,164	\$ 398,164
Shoppers	10,551	167,487
Total goodwill	\$ 408,715	\$ 565,651

As a result of continuing revenue declines in Shoppers, and in conjunction with management's evaluation of the business, the Company determined that a triggering event had occurred and that an interim step-one impairment test of Shoppers' goodwill was warranted in connection with the preparation of its second quarter 2012 financial statements. The fair value of the Shoppers unit was estimated using a discounted cash flow model and a cash flow multiple model, which were consistent with those used in our most recent annual impairment testing as of November 30, 2011. The discounted cash flow and cash flow multiple models utilize projected financial results based on historical performance and management's estimate of future performance, giving consideration to existing and anticipated competitive and economic conditions. The fair value of our Shoppers unit was estimated to be less than its related carrying value. Management determined that the goodwill balance with respect to this reporting unit was impaired and step-two testing was deemed necessary.

Step-two of the goodwill test consists of performing a hypothetical purchase price allocation, under which the estimated fair value of the reporting unit is allocated to its tangible and intangible assets based on their estimated fair values, with any residual amount being assigned to goodwill. During the step-two analysis, book value was estimated to approximate fair value for all working capital items, as well as a number of insignificant assets and liabilities. Owned real estate and buildings were valued using the market approach and comparable property values. Other significant property, plant and equipment items were valued using the cost approach and trending models to estimate the cost of reproduction and then adjusting for the diminution of value from physical deterioration and obsolescence.

## Edgar Filing: HARTE HANKS INC - Form 10-K

The models used to value the total Shoppers unit in step-one relied heavily on management's assumptions. These assumptions, which are significant to the calculated fair values, are considered Level 3 inputs under the

Table of Contents

fair value hierarchy established by FASB ASC 820 as they are unobservable. The assumptions in step-one include discount rate, revenue growth rates, tax rates and operating margins. The discount rate represents the expected return on capital of the Shoppers unit. The discount rate was determined using a target structure of 30% debt and 70% equity. We used the interest rate of a 30-year government security to determine the risk-free rate in our weighted average cost of capital calculation. Projected growth rates and terminal growth rates are primarily driven by management's best estimate of future performance, giving consideration to historical performance and existing and anticipated economic and competitive conditions. Assumed tax rates represent management's best estimates of blended federal and state income tax rates. Operating margin assumptions are primarily driven by management's best estimate of future performance, giving consideration to historical performance and existing and anticipated economic and competitive conditions.

The impairment analysis indicated that \$156.9 million of goodwill was impaired and an impairment charge was recorded in the Consolidated Statements of Comprehensive Income (Loss) in the second quarter of 2012. The Company had not previously recorded any goodwill impairments. Therefore the amount of impairments recorded in the second quarter of 2012 represented the cumulative amount of goodwill impairment charges through June 30, 2012.

We performed our annual goodwill impairment testing for both the Direct Marketing and Shoppers segments as of November 30, 2012. Consistent with prior periods, fair value was determined using a discounted cash flow model, a cash flow multiple model, and with consideration of our overall market capitalization. Based on the results of our November 30, 2012 impairment tests, we did not record any additional impairment losses in 2012 related to goodwill. We did not record an impairment loss related to goodwill in 2011 or 2010.

The Company continues to monitor potential triggering events, including changes in the business climate in which it operates, attrition of key personnel, the current volatility in the capital markets, the Company's market capitalization compared to its book value, the Company's recent operating performance, and the Company's financial projections. The occurrence of one or more triggering events could require additional impairment testing, which could result in additional impairment charges.

A summary of the critical assumptions utilized for our impairment testing in 2012 are outlined below. We believe this information, coupled with our sensitivity analysis, provide relevant information to understand our goodwill impairment testing and evaluate our goodwill balances.

For the annual goodwill impairment tests performed in 2012, we did not significantly change the methodology used in 2011 to determine the fair value of our reporting units. We made changes to certain assumptions utilized in the models for 2011 compared with the prior year due to the U.S. and global economic environments, which affect Direct Marketing, and the economic environments in California and Florida, which affect Shoppers.

Sensitivity Analysis

The following is a sensitivity analysis on the impact of changes in certain assumptions to our overall conclusion concerning impairment of our goodwill balances.

## Edgar Filing: HARTE HANKS INC - Form 10-K

The estimated fair value of our Direct Marketing reporting unit was significantly above its carrying value.

In order to analyze the sensitivity of our assumptions on the results of our Shoppers impairment assessment, we determined the impact that a hypothetical 15% reduction in fair value would have on our conclusions. In the case of our Shoppers reporting unit, a 15% decline in fair value would not result in the reporting unit's carrying value to be in excess of its fair value.

The determination of the recoverability of goodwill requires significant judgment and estimates regarding future cash flows and fair values. These estimates are subject to change and could result in impairment losses being recognized in the future. If different reporting units or different valuation methodologies had been used, the impairment test results could have differed.

Table of Contents

**Stock-based Compensation**

Stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the requisite service period. Determining the fair value of share-based awards requires judgment, including in some cases estimating expected term, volatility and dividend yield. In addition, judgment is required in estimating the amount of stock-based awards that are expected to be forfeited. If actual results differ significantly from some of these estimates, stock-based compensation expense and our results of operations could be materially impacted. For the years ended December 31, 2012, 2011 and 2010, we recorded total stock-based compensation expense of \$3.4 million, \$5.0 million and \$3.9 million, respectively.

**Recent Accounting Pronouncements**

As discussed in Note A of the Notes to Consolidated 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 and are not expected to have a material effect on our consolidated financial statements.

**ITEM 7A. 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 0.21% at December 31, 2012). The five-year 2011 Term Loan Facility has a maturity date of August 16, 2016. At December 31, 2011, our debt balance related to the 2011 Term Loan Facility was \$110.3 million. The three-year \$70 million 2010 Revolving Credit Facility has a maturity date of August 12, 2013. At December 31, 2011, we did not have any debt outstanding under the 2010 Revolving Credit Facility.

Assuming the actual level of borrowings throughout 2012, and assuming a one percentage point change in the average interest rates, we estimate that our net income for 2012 would have changed by approximately \$0.8 million. Due to our overall debt level and cash balance at December 31, 2012, 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 are entered into any interest rate swap or other derivative instruments to hedge the effects of adverse fluctuations in interest rates.

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 sterling, Australian dollar, Philippine peso and Brazilian real. 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

## Edgar Filing: HARTE HANKS INC - Form 10-K

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 (Loss). 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, inter-company transactions that are expected to be settled in the near-term are denominated in

Table of Contents

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 (Loss). Transactions such as these amounted to \$1.6 million in pre-tax currency transaction losses in 2012. 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 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The Financial Statements required to be presented under Item 8 are presented in the Consolidated Financial Statements and the notes thereto beginning at page F-1 of this Form 10-K (Financial Statements).

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

**ITEM 9A. 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 1934 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 1934 Act is 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 fourth quarter of 2012 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



## Edgar Filing: HARTE HANKS INC - Form 10-K

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.

Management's Report on Internal Control Over Financial Reporting and the Report of Independent Registered Public Accounting Firm on the Consolidated Financial Statements and Internal Control Over Financial Reporting are set forth in the Consolidated Financial Statements beginning on page F-1.

Table of Contents

**ITEM 9B. OTHER INFORMATION**

None.

**PART III**

Some of the information required by Items 10 through 14 of this Part III is incorporated by reference from our definitive proxy statement to be filed for our 2013 annual meeting of stockholders (2013 Proxy Statement), as indicated below. Our 2013 Proxy Statement will be filed with the SEC not later than 120 days after December 31, 2012. Because the 2013 Proxy Statement has not yet been finalized and filed, there may be certain discrepancies between the currently anticipated section headings specified below and the final section headings contained in the 2013 Proxy Statement.

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

**Directors and Executive Officers**

The information required by this item regarding our directors and executive officers will be set forth in our 2013 Proxy Statement under the caption **Directors and Executive Officers**, which information is incorporated herein by reference.

**Section 16(a) Compliance**

The information to appear in our 2013 Proxy Statement under the caption **General Information - Section 16(a) Beneficial Ownership Reporting Compliance** is incorporated herein by reference.

**Code of Ethics and Other Governance Information**

The information required by this item regarding the Supplemental Code of Ethics for our Senior Financial Officers (Code of Ethics), audit committee financial experts, audit committee members and procedures for stockholder recommendations of nominees to our Board of Directors will be set forth in our 2013 Proxy Statement under the caption **Corporate Governance**, which information is incorporated herein by reference.

## Edgar Filing: HARTE HANKS INC - Form 10-K

Our Code of Ethics may be found on our website at [www.harte-hanks.com](http://www.harte-hanks.com) by clicking on the link [About Us](#) and then the link [Corporate Governance](#), and a copy of our Code of Ethics is also available in print, without charge, upon written request to Harte-Hanks, Inc., Attn: Corporate Secretary, 9601 McAllister Freeway, Suite 610, San Antonio, Texas 78216. In accordance with the rules of the NYSE and the SEC, we currently intend to disclose any future amendments to our Code of Ethics, or waivers from our Code of Ethics for our Chief Executive Officer, Chief Financial Officer and Controller, by posting such information on our website ([www.harte-hanks.com](http://www.harte-hanks.com)) within the time period required by applicable SEC and NYSE rules.

### **Management Certifications**

In accordance with the Sarbanes-Oxley Act of 2002 and SEC rules thereunder, our Chief Executive Officer and Chief Financial Officer have signed certifications under Sarbanes-Oxley Section 302, which have been filed as exhibits to this Form 10-K. In addition, our Chief Executive Officer submitted his most recent annual certification to the NYSE under Section 303A.12(a) of the NYSE listing standards on June 19, 2012.

Table of Contents

**ITEM 11. EXECUTIVE COMPENSATION**

The information required by this item regarding the compensation of our named executive officers and directors and other required information will be set forth in our 2013 Proxy Statement under the captions Executive Compensation, and Director Compensation, which information is incorporated herein by reference. In accordance with the rules of the SEC, information to be contained in the 2013 Proxy Statement under the caption Compensation Committee Report is not deemed to be filed with the SEC or subject to the liabilities of the 1934 Act.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

**Beneficial Ownership Tables**

The information required by this item regarding security ownership of certain beneficial owners, management and directors will be set forth in our 2013 Proxy Statement under the caption Security Ownership of Management and Principal Stockholders, which information is incorporated herein by reference.

**Equity Compensation Plan Information**

The information required by this item regarding securities authorized for issuance under equity compensation plans will be set forth in our 2013 Proxy Statement under the caption Executive Compensation - Equity Compensation Plan Information at Year-End 2012, which information is incorporated herein by reference.

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

**Transactions with Related Persons**

The information required by this item regarding transactions with related persons, including our policies and procedures for the review, approval or ratification of related person transactions that are required to be disclosed under the SEC's rules and regulations, will be set forth in our 2013 Proxy Statement under the caption Corporate Governance - Certain Relationships and Related Transactions, which information is incorporated herein by reference.

**Director Independence**

The information required by this item regarding director independence will be set forth in our 2013 Proxy Statement under the caption Corporate Governance Independence of Directors, which information is incorporated herein by reference.

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information required by this item regarding the audit committee's pre-approval policies and procedures and the disclosures of fees billed by our principal independent auditor will be set forth in our 2013 Proxy Statement under the caption Audit Committee and Independent Registered Public Accounting Firm, which information is incorporated herein by reference.

Table of Contents

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

**15(a)(1)** Financial Statements

The financial statements filed as part of this report and referenced in Item 8 are presented in the Consolidated Financial Statements and the notes thereto beginning at page F-1 of this Form 10-K (Financial Statements).

**15(a)(2)** Financial Statement Schedules

All schedules for which provision is made in the applicable rules and regulations of the SEC have been omitted as the schedules are not required under the related instructions, are not applicable, or the information required thereby is set forth in the Consolidated Financial Statements or notes thereto.

**15(a)(3)** Exhibits

The Exhibit Index following the Notes to Consolidated Financial Statements in this Form 10-K lists the exhibits that are filed or furnished, as applicable, as part of this Form 10-K.

Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, Harte-Hanks, Inc. has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

HARTE-HANKS, INC.

By: /s/ Larry Franklin  
Larry Franklin  
President and Chief Executive Officer

Date: March 13, 2013

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/s/ Larry Franklin  
Larry Franklin  
Chairman, President and Chief Executive Officer  
Date: March 13, 2013

/s/ Douglas Shepard  
Douglas Shepard  
Executive Vice President and  
Chief Financial Officer  
Date: March 13, 2013

/s/ Jessica Huff  
Jessica Huff  
Vice President, Finance and  
Chief Accounting Officer  
Date: March 13, 2013

/s/ Christopher M. Harte  
Christopher M. Harte, Director  
Date: March 13, 2013

/s/ Houston H. Harte  
Houston H. Harte, Vice Chairman  
Date: March 13, 2013

/s/ Judy C. Odom  
Judy C. Odom, Director  
Date: March 13, 2013

/s/ David L. Copeland  
David L. Copeland, Director  
Date: March 13, 2013

/s/ Karen A. Puckett  
Karen A. Puckett, Director  
Date: March 13, 2013

/s/ William F. Farley  
William F. Farley, Director  
Date: March 13, 2013





Table of Contents

Harte-Hanks, Inc. and Subsidiaries

Index to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm on the Consolidated Financial Statements and Internal Control Over Financial Reporting

Management's Report on Internal Control Over Financial Reporting

Consolidated Balance Sheets as of December 31, 2012 and 2011

Consolidated Statements of Comprehensive Income (Loss) for each of the years in the three-year period ended December 31, 2012

Consolidated Statements of Cash Flows for each of the years in the three-year period ended December 31, 2012

Consolidated Statements of Changes in Equity for each of the years in the three-year period ended December 31, 2012

Notes to Consolidated Financial Statements

All schedules for which provision is made in the applicable rules and regulations of the SEC have been omitted as the schedules are not required under the related instructions, are not applicable, or the information required thereby is set forth in the consolidated financial statements or notes thereto.

Table of Contents

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

Harte-Hanks, Inc.:

We have audited the accompanying consolidated balance sheets of Harte-Hanks, Inc. and subsidiaries (the Company) as of December 31, 2012 and 2011, and the related consolidated statements of comprehensive income (loss), changes in equity, and cash flows for each of the years in the three-year period ended December 31, 2012. We also have audited the Company's internal control over financial reporting as of December 31, 2012, based on criteria established in Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Harte-Hanks, Inc. and subsidiaries as of December 31, 2012 and 2011, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2012, in conformity with U.S. generally accepted accounting principles. Also in our opinion, Harte-Hanks, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on

Edgar Filing: HARTE HANKS INC - Form 10-K

criteria established in Internal Control Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission.

/s/ KPMG LLP

San Antonio, Texas

March 13, 2013

F-2

---

Table of Contents

Management's Report on Internal Control Over Financial Reporting

We are responsible for the preparation and integrity of the consolidated financial statements appearing in our Annual Report. The consolidated financial statements were prepared in conformity with U.S. generally accepted accounting principles and include amounts based on management's estimates and judgments. All other financial information in this report has been presented on a basis consistent with the information included in the consolidated financial statements.

We are also responsible for establishing and maintaining adequate internal control over financial reporting. We maintain a system of internal control that is designed to provide reasonable assurance as to the fair and reliable preparation and presentation of the consolidated financial statements, as well as to safeguard assets from unauthorized use or disposition.

Our control environment is the foundation for our system of internal control over financial reporting. It sets the tone of our organization and includes factors such as integrity and ethical values. Our internal control over financial reporting is supported by formal policies and procedures that are reviewed, modified and improved as changes occur in business conditions and operations.

The Audit Committee of the Board of Directors, which is composed solely of outside directors, meets periodically with members of management, the internal auditors and the independent auditors to review and discuss internal controls over financial reporting and accounting and financial reporting matters. Our independent registered public accounting firm and internal auditors report to the Audit Committee and accordingly have full and free access to the Audit Committee at any time.

We conducted an evaluation of the effectiveness of our internal control over financial reporting based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. This evaluation included review of the documentation of controls, evaluation of the design effectiveness of controls, testing of the operating effectiveness of controls and a conclusion on this evaluation. Based on our evaluation, we concluded that our internal control over financial reporting was effective as of December 31, 2012.

KPMG LLP, an independent registered public accounting firm, has issued a report on the effectiveness of the Company's internal control over financial reporting, which is included on pages F-2 and F-3 of this Form 10-K.

March 13, 2013

/s/ Larry Franklin  
Larry Franklin  
President and Chief Executive Officer

/s/ Douglas Shepard  
Douglas Shepard  
Executive Vice President and  
Chief Financial Officer

/s/ Jessica Huff  
Jessica Huff  
Vice President, Finance and  
Chief Accounting Officer

F-3

---

Edgar Filing: HARTE HANKS INC - Form 10-K

Table of Contents

Harte-Hanks, Inc. and Subsidiaries Consolidated Balance Sheets

In thousands, except per share and share amounts	December 31,	
	2012	2011
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 49,648	\$ 86,778
Accounts receivable ( <i>less allowance for doubtful accounts of \$3,402 at December 31, 2012 and \$3,230 at December 31, 2011</i> )	141,347	154,333
Inventory	5,067	5,680
Prepaid expenses	9,178	8,781
Current deferred income tax asset	8,181	9,590
Prepaid income tax	4,491	0
Other current assets	7,588	6,476
Total current assets	225,500	271,638
Total assets of discontinued operations	0	16,188
Property, plant and equipment		
Land	2,299	2,288
Buildings and improvements	33,767	34,221
Software	92,974	94,755
Equipment and furniture	158,639	157,404
Software development and equipment installations in progress	5,459	3,170
Gross property, plant and equipment	293,138	291,838
Less accumulated depreciation and amortization	(231,167)	(222,946)
Net property, plant and equipment	61,971	68,892
Goodwill	408,715	565,651
Other intangible assets ( <i>less accumulated amortization of \$9,541 at December 31, 2012 and \$9,296 at December 31, 2011</i> )	5,259	5,504
Other assets	4,767	4,640
Total assets	\$ 706,212	\$ 932,513
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities		
Current maturities of long-term debt	\$ 12,250	\$ 69,188
Accounts payable	42,187	45,588
Accrued payroll and related expenses	16,777	21,941
Deferred revenue and customer advances	36,924	36,575
Income taxes payable	1,518	4,594
Customer postage and program deposits	19,892	15,759
Other current liabilities	10,649	10,005
Total current liabilities	140,197	203,650
Total liabilities of discontinued operations	0	1,441
Long-term debt	98,000	110,250
Other long-term liabilities ( <i>including deferred income taxes of \$53,935 at December 31, 2012 and \$92,448 at December 31, 2011</i> )	139,851	170,817
Total liabilities	378,048	486,158
Stockholders' equity		
Common stock, \$1 par value, 250,000,000 shares authorized. 118,737,456 shares issued at December 31, 2012 and 118,487,455 shares issued at December 31, 2011	118,737	118,487
Additional paid-in capital	341,586	341,149

Edgar Filing: HARTE HANKS INC - Form 10-K

Retained earnings	1,165,952	1,276,266
Less treasury stock, 56,348,026 shares at cost at December 31, 2012 and 55,668,137 shares at cost at December 31, 2011	(1,248,377)	(1,244,224)
Accumulated other comprehensive loss	(49,734)	(45,323)
Total stockholders' equity	328,164	446,355
Total liabilities and stockholders' equity	\$ 706,212	\$ 932,513

See Accompanying Notes to Consolidated Financial Statements.

F-4

---

Edgar Filing: HARTE HANKS INC - Form 10-K

Table of Contents

Harte-Hanks, Inc. and Subsidiaries Consolidated Statements of Comprehensive Income (Loss)

In thousands, except per share amounts	Year Ended December 31,		
	2012	2011	2010
Operating revenues	\$ 767,709	\$ 811,636	\$ 820,720
Operating expenses			
Labor	332,784	348,637	342,434
Production and distribution	282,743	300,703	299,228
Advertising, selling, general and administrative	64,765	64,347	64,079
Impairment of goodwill	156,936	0	0
Depreciation and software amortization	20,176	19,622	21,443
Intangible asset amortization	245	229	290
Total operating expenses	857,649	733,538	727,474
Operating income (loss)	(89,940)	78,098	93,246
Other expenses (income)			
Interest expense	3,574	3,184	2,824
Interest income	(91)	(249)	(200)
Other, net	2,863	(1,505)	2,136
	6,346	1,430	4,760
Income (loss) from continuing operations before income taxes	(96,286)	76,668	88,486
Income tax expense (benefit)	(23,182)	30,791	33,292
Income (loss) from continuing operations	(73,104)	45,877	55,194
Loss from discontinued operations, net of income taxes	(7,533)	(1,679)	(1,590)
Loss on sale, net of income taxes	(2,716)	0	0
Total discontinued operations	(10,249)	(1,679)	(1,590)
Net income (loss)	\$ (83,353)	\$ 44,198	\$ 53,604
Basic earnings (loss) per common share			
Continuing operations	\$ (1.16)	\$ 0.73	\$ 0.87
Discontinued operations	\$ (0.17)	\$ (0.03)	\$ (0.03)
Basic earnings (loss) per common share	\$ (1.33)	\$ 0.70	\$ 0.84
Weighted-average common shares outstanding	62,887	63,173	63,616
Diluted earnings (loss) per common share			
Continuing operations	\$ (1.16)	\$ 0.72	\$ 0.86
Discontinued operations	\$ (0.17)	\$ (0.02)	\$ (0.02)
Diluted earnings (loss) per common share	\$ (1.33)	\$ 0.70	\$ 0.84
Weighted-average common and common equivalent shares outstanding	62,887	63,552	64,139
Other comprehensive income (loss), net of tax			
Adjustment to pension liability	\$ (5,726)	\$ (10,304)	\$ (1,576)
Foreign currency translation adjustments	1,315	(1,337)	(136)
Total other comprehensive loss, net of tax	(4,411)	(11,641)	(1,712)
Comprehensive income (loss)	\$ (87,764)	\$ 32,557	\$ 51,892

See Accompanying Notes to Consolidated Financial Statements.





Edgar Filing: HARTE HANKS INC - Form 10-K

Table of Contents

Harte-Hanks, Inc. and Subsidiaries Consolidated Statements of Cash Flows

In thousands	Year Ended December 31,		
	2012	2011	2010
<b>Cash Flows from Operating Activities</b>			
Net income (loss)	\$ (83,353)	\$ 44,198	\$ 53,604
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Loss from discontinued operations	12,514	2,696	2,159
Loss on sale of discontinued operations	4,863	0	0
Impairment of goodwill	156,936	0	0
Depreciation and software amortization	20,176	19,622	21,443
Intangible asset amortization	245	229	290
Stock-based compensation	3,412	4,988	3,907
Excess tax benefits from stock-based compensation	(57)	(215)	0
Net pension cost (payments)	158	(175)	(1,531)
Deferred income taxes	(43,515)	10,387	7,369
Other, net	36	(2,162)	186
Changes in operating assets and liabilities, net of acquisitions:			
Decrease (increase) in accounts receivable, net	12,986	(5,258)	(9,314)
Decrease (increase) in inventory	613	238	(1,714)
Increase in prepaid expenses and other current assets	(1,510)	(197)	(382)
(Decrease) increase in accounts payable	(3,401)	(9,357)	12,162
(Decrease) increase in other accrued expenses and other liabilities	(8,008)	(2,105)	6,499
Other, net	(248)	(1,182)	232
Net cash provided by continuing operations	71,847	61,707	94,910
Net cash provided by (used in) discontinued operations	4,476	(1,042)	959
Net cash provided by operating activities	76,323	60,665	95,869
<b>Cash Flows from Investing Activities</b>			
Acquisitions, net of cash acquired	0	0	(12,904)
Purchases of property, plant and equipment	(13,856)	(20,970)	(17,201)
Proceeds from the sale of property, plant and equipment	98	3,483	84
Net cash flows from investing activities within discontinued operations	(86)	(64)	(125)
Net cash used in investing activities	(13,844)	(17,551)	(30,146)
<b>Cash Flows from Financing Activities</b>			
Borrowings	0	122,500	0
Repayment of borrowings	(69,188)	(136,062)	(46,688)
Debt financing costs	(0)	(811)	(491)
Issuance of common stock	660	713	75
Excess tax benefits from stock-based compensation	57	215	0
Purchase of treasury stock	(4,402)	(8,363)	0
Dividends paid	(26,961)	(20,370)	(19,141)
Net cash used in financing activities	(99,834)	(42,178)	(66,245)
Effect of exchange rate changes on cash and cash equivalents	225	(154)	(80)
Net increase (decrease) in cash and cash equivalents	(37,130)	782	(602)
Cash and cash equivalents at beginning of year	86,778	85,996	86,598
Cash and cash equivalents at end of year	\$ 49,648	\$ 86,778	\$ 85,996

See Accompanying Notes to Consolidated Financial Statements.

F-6

---

Edgar Filing: HARTE HANKS INC - Form 10-K

Table of Contents

Harte-Hanks, Inc. and Subsidiaries Consolidated Statements of Changes in Equity

In thousands, except per share amounts	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
Balance at December 31, 2009	\$ 118,243	\$ 333,612	\$ 1,217,975	\$ (1,236,217)	\$ (31,970)	\$ 401,643
Exercise of stock options and release of nonvested shares	53	22	0	(124)	0	(49)
Net tax effect of stock options exercised and release of nonvested shares	0	(588)	0	0	0	(588)
Stock-based compensation	0	3,907	0	0	0	3,907
Dividends paid (\$0.30 per share)	0	0	(19,141)	0	0	(19,141)
Treasury stock issued	0	(158)	0	317	0	159
Net income	0	0	53,604	0	0	53,604
Other comprehensive loss	0	0	0	0	(1,712)	(1,712)
Balance at December 31, 2010	\$ 118,296	\$ 336,795	\$ 1,252,438	\$ (1,236,024)	\$ (33,682)	\$ 437,823
Exercise of stock options and release of nonvested shares	191	522	0	(193)	0	520
Net tax effect of stock options exercised and release of nonvested shares	0	(959)	0	0	0	(959)
Stock-based compensation	0	4,988	0	0	0	4,988
Dividends paid (\$0.32 per share)	0	0	(20,370)	0	0	(20,370)
Treasury stock issued	0	(197)	0	356	0	159
Purchase of treasury stock	0	0	0	(8,363)	0	(8,363)
Net income	0	0	44,198	0	0	44,198
Other comprehensive loss	0	0	0	0	(11,641)	(11,641)
Balance at December 31, 2011	\$ 118,487	\$ 341,149	\$ 1,276,266	\$ (1,244,224)	\$ (45,323)	\$ 446,355
Exercise of stock options and release of nonvested shares	250	410	0	(205)	0	455
Net tax effect of stock options exercised and release of nonvested shares	0	(3,082)	0	0	0	(3,082)
Stock-based compensation	0	3,412	0	0	0	3,412
Dividends paid (\$0.43 per share)	0	0	(26,961)	0	0	(26,961)
Treasury stock issued	0	(303)	0	454	0	151
Purchase of treasury stock	0	0	0	(4,402)	0	(4,402)
Net loss	0	0	(83,353)	0	0	(83,353)
Other comprehensive loss	0	0	0	0	(4,411)	(4,411)
Balance at December 31, 2012	\$ 118,737	\$ 341,586	\$ 1,165,952	\$ (1,248,377)	\$ (49,734)	\$ 328,164

See Accompanying Notes to Consolidated Financial Statements.

Table of Contents

**Harte-Hanks, Inc. and Subsidiaries Notes to Consolidated Financial Statements**

**Note A Significant Accounting Policies**

**Consolidation**

The accompanying consolidated financial statements present the financial position and the results of operations and cash flows of Harte-Hanks, Inc. and its subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

As used in this report, the terms Harte-Hanks, we, us, or our may refer to Harte-Hanks, one or more of its consolidated subsidiaries, or all of them taken as a whole.

**Discontinued Operations**

As discussed in Note P, *Discontinued Operations*, we sold the assets of our Florida Shoppers operations on December 31, 2012. The operating results and related balances of our Florida Shoppers, including the loss on the sale, are being reported as discontinued operations in the Consolidated Financial Statements. Unless otherwise stated, amounts related to the Florida Shoppers operations are excluded from the Notes to Consolidated Financial Statements for all years presented.

**Reclassification of Prior Year Amounts**

Certain prior year amounts have been reclassified for comparative purposes. In the Consolidated Balance Sheets, amounts related to postage advances from our Direct Marketing customers were previously included in the line item Other current liabilities. These postage advances are now being disclosed as a separate line item titled Customer postage and program deposits. Previously we had disclosed these postage advance amounts in our Notes to Consolidated Financial Statements.

**Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (U.S. GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results and outcomes could differ from those estimates and assumptions. On an ongoing basis, management reviews its estimates based on currently available information. Changes in facts and

circumstances could result in revised estimates and assumptions.

#### **Operating Expense Presentation in Consolidated Statements of Comprehensive Income (Loss)**

The Labor line in the Consolidated Statements of Comprehensive Income (Loss) includes all employee payroll and benefits, including stock-based compensation, along with temporary labor costs. The Production and distribution and Advertising, selling, general and administrative lines do not include labor, depreciation or amortization.

#### **Revenue Recognition**

We recognize revenue when all of the following criteria are satisfied: (i) persuasive evidence of an arrangement exists; (ii) the price is fixed or determinable; (iii) collectability is reasonably assured; and (iv) the service has been performed or the product has been delivered.

Payments received in advance of the performance of services or delivery of the product are recorded as deferred revenue until such time as the services are performed or the product is delivered.

Our accounting policy for revenue recognition has an impact on our reported results and relies on certain estimates that require judgments on the part of management. The portion of our revenue that is most subject to estimates and judgments is revenue recognized using the proportional performance method, as discussed below.

Table of Contents

Direct Marketing revenue is derived from a variety of services and products, and may be billed at hourly rates, monthly rates or a fixed price. For all sales, we require either a purchase order, a statement of work signed by the client, a written contract, or some other form of written authorization from the client.

Revenue from agency and creative services, analytical services and market research is typically billed based on time and materials or at a fixed price. If billed at a fixed price, revenue is recognized on a proportional performance basis as the services specified in the arrangement are performed. In most cases, proportional performance is based on the ratio of direct costs incurred to total estimated costs where the costs incurred, primarily labor hours and outsourced services, represent a reasonable surrogate for output measures or contract performance. For fixed fee market research revenue streams, revenue is recognized in proportion to the value of service provided based on output criteria.

Revenue from email marketing, social media marketing and other digital solutions is recognized as the work is performed. Revenue from these services is typically based on a fixed price or rate given to the client.

Revenue associated with new marketing database builds is deferred until complete or until client acceptance. Upon completion or acceptance, revenue and direct build costs are then recognized over the term of the related arrangement as the services are provided. Revenue from database and website hosting services is recognized ratably over the contractual hosting period. Pricing for database builds are typically based on a fixed price and hosting fees are typically based on a fixed price per month or per contract.

Revenue from technology database subscriptions is based on a fixed price and is recognized ratably over the term of the subscription. Revenue from stand-alone technology data sales is recognized at the time of delivery.

Revenue from services such as data processing, printing, personalization of communication pieces using laser and inkjet printing, targeted mail, and transportation logistics is recognized as the work is performed. Revenue from these services is typically based on a fixed price or rate given to the client. Postage costs of mailings in our direct mail business are borne by our clients and are not directly reflected in our revenues or expenses.

Revenue related to fulfillment and contact centers, including inbound and outbound calling and email management, is also typically based on a fixed price per transaction or service provided. Revenue from these services is recognized as the service or activity is performed.

Revenue from software arrangements involving multiple elements is allocated to each element based on the vendor-specific objective evidence of fair values of the respective elements. For software sales with multiple elements (for example, software licenses with undelivered post-contract customer support or PCS ), we allocate revenue to each component of the arrangement using the residual value method based on the fair value of the undelivered elements. This means we defer revenue from the software sale equal to the fair value of the undelivered elements. The fair value of PCS is based upon separate sales of renewals to other clients. The fair value of services, such as training and consulting, is based upon separate sales of these services to other clients.

## Edgar Filing: HARTE HANKS INC - Form 10-K

The revenue allocated to PCS is recognized ratably over the term of the support period. Revenue allocated to professional services is recognized as the services are performed. The revenue allocated to software products, including time-based software licenses, is recognized, if collection is probable, upon execution of a licensing agreement and shipment of the software or ratably over the term of the license, depending on the structure and terms of the arrangement. If the licensing agreement is for a term of a year or less and includes PCS, we recognize the software and the PCS revenue ratably over the term of the license.

For certain non-software arrangements, we enter into contracts that include delivery of a combination of our service offerings. Such arrangements are divided into separate units of accounting, provided that the delivered element(s) has stand-alone value and objective and reliable evidence of the fair value of the undelivered element(s) exist(s).

F-9

---



Table of Contents

When we are able to unbundle the arrangement into separate units of accounting, revenue from each service is recognized separately, and in accordance with our revenue recognition policy for each element. If we are unable to unbundle the arrangement into separate units of accounting, we apply one of the revenue recognition policies to the entire arrangement. This might impact the timing of revenue recognition, but would not change the total revenue recognized from the arrangement.

Shopper services are considered rendered, and the revenue recognized, when all printing, sorting, labeling and ancillary services have been provided and the mailing material has been received by the USPS.

Taxes collected from customers and remitted to governmental authorities are not reflected in our revenues or expenses.

**Cash Equivalents**

All highly liquid investments with an original maturity of 90 days or less at the time of purchase are considered to be cash equivalents. Cash equivalents are carried at cost, which approximates fair value.

**Allowance for Doubtful Accounts**

We maintain our allowance for doubtful accounts at a balance adequate to reduce accounts receivable to the amount of cash expected to be realized upon collection. The methodology used to determine the minimum allowance balance is based on our prior collection experience and is generally related to the accounts receivable balance in various aging categories. The balance is also influenced by specific clients' financial strength and circumstance. Accounts that are determined to be uncollectible are written off in the period in which they are determined to be uncollectible. Periodic changes to the allowance balance are recorded as increases or decreases to bad debt expense, which is included in the Advertising, selling, general and administrative line of our Consolidated Statements of Comprehensive Income (Loss). The changes in the allowance for doubtful accounts consisted of the following:

In thousands	Year Ended December 31,		
	2012	2011	2010
Balance at beginning of year	\$ 3,230	\$ 3,096	\$ 2,784
Additions charged to expense	1,099	1,396	1,602
Amounts recovered against the allowance, net of charges	(927)	(1,262)	(1,290)
Balance at end of year	\$ 3,402	\$ 3,230	\$ 3,096

**Inventory**

Inventory, consisting primarily of newsprint, job paper and operating supplies, is stated at the lower of cost (first-in, first-out method) or market.

**Property, Plant and Equipment**

Property, plant and equipment are stated on the basis of cost. Depreciation is computed using the straight-line method at rates calculated to amortize the cost of the assets over their useful lives. The general ranges of estimated useful lives are:

Buildings and improvements	10 to 40 years
Software	3 to 10 years
Equipment and furniture	3 to 20 years

Long-lived assets such as property, plant and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In the second quarter of 2012 we wrote off \$0.6 million of software related to various unprofitable digital initiatives in our Shoppers business, including SaverTime and mobile apps. The discontinuance of these initiatives was part of our continued efforts to

Table of Contents

reduce expenses in our Shoppers business as a result of our financial performance and the poor economic conditions in the areas in which our Shoppers operate. We did not record an impairment of long-lived assets in 2011 or 2010.

In December 2011 we sold a vacant piece of land adjacent to our Shoppers Brea, California facility for \$3.4 million. We recognized a gain of \$2.3 million on this transaction.

Property, plant and equipment includes capital lease assets. Capital lease assets at December 31, 2012 and 2011 consisted of:

In thousands	December 31,	
	2012	2011
Equipment and furniture	\$ 2,774	\$ 2,749
Less accumulated amortization	(1,604)	(1,606)
Net book value	\$ 1,170	\$ 1,143

Amortization expense related to capital lease assets was \$0.5 million, \$0.4 million and \$0.6 million for the years ended December 31, 2012, 2011 and 2010, respectively.

Depreciation and amortization on the remaining property plant and equipment was \$19.6 million, \$19.2 million and \$20.8 million for the years ended December 31, 2012, 2011 and 2010, respectively.

**Goodwill and Other Intangibles**

Goodwill is recorded to the extent that the purchase price of an acquisition exceeds the fair value of the identifiable net assets acquired. Other intangibles with definite and indefinite useful lives are recorded at fair value at the date of the acquisition. The Company tests its goodwill and other intangible assets with indefinite useful lives for impairment as of November 30 of each year and as of an interim date should factors or indicators become apparent that would require an interim test. The company assesses the impairment of its goodwill by determining the fair value of each of its reporting units and comparing the fair value to the carrying value for each reporting unit. Fair values of our reporting units and other intangibles with indefinite useful lives have been determined using discounted cash flow and cash flow multiple methodologies. Our overall market capitalization also was considered when evaluating the fair values of our reporting units. Intangible assets with definite useful lives are amortized over their respective estimated useful lives and reviewed for impairment if we believe that changes or triggering events have occurred that could have caused the carrying value of the intangible assets to exceed its fair value. As a result of continuing revenue declines in Shoppers, and in conjunction with management's evaluation of the business, the Company determined that a triggering event had occurred in the second quarter of 2012. The subsequent goodwill impairment testing resulted in impairment charges in the second quarter of 2012 of \$156.9 million. We also recorded \$8.4 million in impairment charges related to trade names and client relationships associated with the Tampa Flyer, which are part of the Florida Shoppers operations and included in discontinued operations. We have not recorded any other impairments of goodwill or other intangible assets in our continuing operations in any of the years during the three-year period ended December 31, 2012.

**Income Taxes**

Income taxes are calculated using the asset and liability method. Deferred income taxes are recognized for the tax consequences resulting from temporary differences by applying enacted statutory tax rates applicable to future years. These temporary differences are associated with differences between the financial and the tax basis of existing assets and liabilities. Any statutory change in tax rates will be recognized immediately in deferred taxes and income.

### **Earnings Per Share**

Basic earnings per common share are based upon the weighted-average number of common shares outstanding during the period. Diluted earnings per common share are based upon the weighted-average number of common shares and dilutive common stock equivalents outstanding during the period. Dilutive common stock equivalents are calculated based on the assumed exercise of stock options and vesting of non-vested shares using the treasury stock method.

Table of Contents

**Stock-Based Compensation**

All share-based awards are recognized as operating expense in the Labor line of the Consolidated Statements of Comprehensive Income (Loss). Calculated expense is based on the fair values of the awards on the date of grant and is recognized over the requisite service period.

**Reserve for Healthcare, Workers Compensation, Automobile and General Liability**

We are self-insured for our workers compensation, automobile, general liability and a portion of our healthcare insurance. We make various subjective judgments about a number of factors in determining our reserve for healthcare, workers compensation, automobile and general liability insurance, and the related expense. Our deductible for individual healthcare claims is \$0.3 million. Our deductible for workers compensation is \$0.5 million. We have a \$0.3 million deductible for automobile and general liability claims. Our insurance administrator provides us with estimated loss reserves, based upon its experience dealing with similar types of claims, as well as amounts paid to date against these claims. We apply actuarial factors to both insurance estimated loss reserves and to paid claims and then determine reserve levels, taking into account these calculations. At December 31, 2012 and 2011, our reserve for healthcare, workers compensation, automobile and general liability was \$11.4 million and \$12.1 million, respectively. Periodic changes to the reserve for workers compensation, automobile and general liability are recorded as increases or decreases to insurance expense, which is included in the Advertising, selling, general and administrative line of our Consolidated Statements of Comprehensive Income (Loss). Periodic changes to the reserve for healthcare are recorded as increases or decreases to employee benefits expense, which is included in the Labor line of our Consolidated Statements of Comprehensive Income (Loss).

**Foreign Currencies**

In most instances the functional currencies of our foreign operations are the local currencies. Assets and liabilities recorded in foreign currencies are translated in U.S. dollars at the exchange rate on the balance sheet date. Revenue and expenses are translated at average rates of exchange prevailing during a given month. Adjustments resulting from this translation are charged or credited to other comprehensive loss.

**Recent Accounting Pronouncements**

In the first quarter of 2012, we adopted Accounting Standards Updates (ASU) 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income*. ASU 2011-05 eliminates the option to present other comprehensive income in the statement of changes in equity and provides the option to present the components of net income and comprehensive income in either one combined financial statement or two consecutive financial statements. We previously presented the components of comprehensive income in our Consolidated Statements of Stockholders Equity and Comprehensive Income (now titled Consolidated Statements of Changes in Equity). In connection with this adoption we have presented the components of net income and comprehensive income in one combined financial statement, the Consolidated Statements of Comprehensive Income (Loss). The adoption of ASU 2011-05 did not affect our operating results, cash flows or financial position.

## Edgar Filing: HARTE HANKS INC - Form 10-K

In the third quarter of 2012, the Financial Accounting Standards Board (FASB) issued ASU No. 2012-02, *Intangibles - Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment* (ASU 2012-12). ASU 2012-02 allows an entity to first assess qualitative factors to determine whether it is necessary to perform the quantitative impairment test for indefinite-lived intangible assets. An organization that elects to perform a qualitative assessment is required to perform the quantitative impairment test for an indefinite-lived intangible asset if it is more likely than not that the asset is impaired. We plan to adopt ASU 2012-02 in the first quarter of 2013. The adoption of ASU 2012-02 will not affect our operating results, cash flows or financial position.

### **Note B Acquisitions**

On August 31, 2010, we acquired Information Arts (UK) Limited (Information Arts). Based in the United Kingdom, Information Arts is a provider of data-driven marketing insight to business-to-business marketers across Europe and

Table of Contents

increasingly across the globe. Information Arts delivers data to improve multichannel marketing effectiveness. This insight is derived from profiling, segmentation, modeling and other analytics, and drives engagements that include marketing data management, data hygiene, data acquisition and data planning. Information Arts and Harte-Hanks' other marketing offerings in Europe are being combined to deliver multichannel Demand Center solutions - integrated lead generation and lead management programs. Goodwill of \$12.8 million and intangible assets subject to amortization of \$0.5 million have been recognized in this transaction and assigned to the Direct Marketing segment.

The total cost of the acquisition in 2010 was \$12.9 million, all paid in cash. The operating results of this acquisition have been included in the accompanying Consolidated Financial Statements from the date of the acquisition. We did not make any acquisitions in 2012 or 2011.

We have not disclosed proforma amounts including the operating results of this acquisition as the effect on our operating results is not considered material.

**Note C Fair Value of Financial Instruments**

FASB ASC 820, *Fair Value Measurements and Disclosures*, (ASC 820) defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 also establishes a fair value hierarchy that prioritizes the inputs used in valuation methodologies into three levels:

**Level 1** Quoted prices in active markets for identical assets or liabilities.

**Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

**Level 3** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Because of their maturities and/or variable interest rates, certain financial instruments have fair values approximating their carrying values. These instruments include cash and cash equivalents, accounts receivable and trade payables. The fair value of our outstanding debt is disclosed in Note D, *Long-Term Debt*. The fair value of the assets in our funded pension plan is disclosed in Note G, *Employee Benefit Plans*. As discussed in Note F, *Goodwill and Other Intangible Assets*, in the second quarter of 2012, the fair value of our Shoppers unit was calculated in relation to a step-one impairment analysis, and the fair value of Shoppers' PP&E, goodwill and other intangible assets were calculated in relation to a step-two impairment analysis.

**Note D Long-Term Debt**

Our long-term debt obligations at year-end were as follows:

<b>In thousands</b>	<b>December 31,</b>	
	<b>2012</b>	<b>2011</b>
2008 Term Loan Facility, various interest rates based on LIBOR, due March 7, 2012	0	60,000
2010 Revolving Credit Facility, various interest rates based on LIBOR, due August 12, 2013 (\$60.5 million capacity at December 31, 2012)	0	0
2011 Term Loan Facility, various interest rates based on LIBOR (effective rate of 2.21% at December 31, 2012), due August 16, 2016	110,250	119,438
Total debt	110,250	179,438
Less current maturities	12,250	69,188
Total long-term debt	\$ 98,000	\$ 110,250



Table of Contents

The carrying values and estimated fair values of our outstanding debt at year-end were as follows:

In thousands	December 31,			
	2012		2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Total debt	\$ 110,250	\$ 110,250	\$ 179,438	\$ 179,286

The estimated fair values were calculated using current rates provided to us by our bankers for debt of the same remaining maturity and characteristics. These current rates are considered Level 2 inputs under the fair value hierarchy established by FASB ASC 820, *Fair Value Measurements and Disclosures*, (ASC 820).

**Credit Facilities**

On March 7, 2008, we entered into a four-year \$100 million term loan facility (2008 Term Loan Facility) with Wells Fargo Bank, N.A., as Administrative Agent. The 2008 Term Loan Facility matured on March 7, 2012, at which time we paid the remaining outstanding principal of \$60.0 million using cash on hand.

On August 12, 2010, we entered into a three-year \$70 million revolving credit facility, which includes a \$25 million accordion feature, a \$25 million letter of credit sub-facility and a \$5 million swing line loan sub-facility (2010 Revolving Credit Facility), with Bank of America, N.A., as Administrative Agent. The 2010 Revolving Credit Facility permits us to request up to a \$25 million increase in the total amount of the facility. The 2010 Revolving Credit Facility matures on August 12, 2013. For each borrowing under the 2010 Revolving Credit Facility, we can generally choose to have the interest rate for that borrowing calculated on either (i) the LIBOR rate (as defined in the 2010 Revolving Credit Facility) for the applicable interest period, plus a spread which is determined based on our total net debt-to-EBITDA ratio (as defined in the 2010 Revolving Credit Facility) then in effect, which ranges from 2.25% to 3.00% per annum; or (ii) the highest of (a) the Federal Funds Rate plus 0.50%, (b) the Agent's prime rate, and (c) the LIBOR rate plus 1.00%, plus a spread which is determined based on our total net debt-to-EBITDA ratio then in effect, which ranges from 1.25% to 2.00% per annum. There is a facility fee that we are also required to pay under the 2010 Revolving Credit Facility. The facility fee rate ranges from 0.40% to 0.45% per annum, depending on our total net debt-to-EBITDA ratio then in effect. In addition, there is 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 LIBOR 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 2010 Revolving Credit Facility at any time without incurring any prepayment penalties. At December 31, 2012 we had letters of credit totaling \$9.5 million issued under the 2010 Revolving Credit Facility, decreasing the amount available for borrowing to \$60.5 million. Our 2010 Revolving Credit Facility matures in August 2013. We believe that we will be able to obtain a replacement revolver facility in a similar amount and with similar terms.

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.

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 3.0 to 1. The credit facilities also contain customary covenants restricting our and our subsidiaries' ability to:

F-14

---

## Edgar Filing: HARTE HANKS INC - Form 10-K

### Table of Contents

- 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 20% of the consolidated revenue, assets or EBITDA 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.

The future minimum principal payments related to our debt at December 31, 2012 are as follows:

<b>In thousands</b>	
2013	\$ 12,250
2014	15,313
2015	18,375
2016	64,312
2017	0
	\$ 110,250

Cash payments for interest were \$3.2 million, \$3.2 million, and \$2.8 million for the years ended December 31, 2012, 2011 and 2010, respectively.

### **Note E Income Taxes**

The components of income tax expense (benefit) are as follows:

Edgar Filing: HARTE HANKS INC - Form 10-K

In thousands	Year Ended December 31,		
	2012	2011	2010
<b>Current</b>			
Federal	\$ 14,505	\$ 12,507	\$ 20,296
State and local	3,950	5,843	4,009
Foreign	1,878	2,054	1,618
Total current	\$ 20,333	\$ 20,404	\$ 25,923
<b>Deferred</b>			
Federal	\$ (34,916)	\$ 10,267	\$ 7,830
State and local	(7,721)	237	(146)
Foreign	(878)	(117)	(315)
Total deferred	\$ (43,515)	\$ 10,387	\$ 7,369
Total income tax expense (benefit)	\$ (23,182)	\$ 30,791	\$ 33,292

F-15

Edgar Filing: HARTE HANKS INC - Form 10-K

Table of Contents

The United States and foreign components of income (loss) from continuing operations before income taxes were as follows:

In thousands	Year Ended December 31,		
	2012	2011	2010
United States	\$ (100,191)	\$ 69,941	\$ 83,388
Foreign	3,905	6,727	5,098
Total income (loss) from continuing operations before income taxes	\$ (96,286)	\$ 76,668	\$ 88,486

The differences between total income tax expense (benefit) and the amount computed by applying the statutory federal income tax rate to income before income taxes were as follows:

In thousands	2012		Year Ended December 31,		2010	
		Rate	2011	Rate		Rate
Computed expected income tax expense (benefit)	\$ (33,700)	-35%	\$ 26,834	35%	\$ 30,970	35%
Net effect of state income taxes	2,907	3%	3,952	5%	2,290	3%
Production activities deduction	0	0%	0	0%	(469)	-1%
Goodwill impairment	8,765	9%	0	0%	0	0%
Change in beginning of year valuation allowance	(1,225)	-1%	(117)	0%	40	0%
Other, net	71	0%	122	0%	461	1%
Income tax expense (benefit) for the period	\$ (23,182)	-24%	\$ 30,791	40%	\$ 33,292	38%

Total income tax expense (benefit) was allocated as follows:

In thousands	Year Ended December 31,		
	2012	2011	2010
Continuing operations	\$ (23,182)	\$ 30,791	\$ 33,292
Discontinued operations	(4,981)	(1,016)	(569)
Loss on sale	(2,147)	0	0
Stockholders' equity	(736)	(5,910)	(463)
Total	\$ (31,046)	\$ 23,865	\$ 32,260

The tax effects of temporary differences that gave rise to significant portions of the deferred tax assets and deferred tax liabilities were as follows:

In thousands	December 31,	
	2012	2011
<b>Deferred tax assets</b>		
Deferred compensation and retirement plan	\$ 31,515	\$ 27,039
Accrued expenses not deductible until paid	5,459	6,570
Employee stock-based compensation	4,000	6,426
Accrued payroll not deductible until paid	2,363	3,573

Edgar Filing: HARTE HANKS INC - Form 10-K

Accounts receivable, net		1,963		1,221
Other, net		158		185
State income tax		69		494
Federal net operating loss carryforwards		151		151
Foreign net operating loss carryforwards		2,439		2,590
State net operating loss carryforwards		2,214		1,206
Total gross deferred tax assets		50,331		49,455
Less valuation allowance		(2,439)		(3,638)
Net deferred tax assets	\$	47,892	\$	45,817
<b>Deferred tax liabilities</b>				
Property, plant and equipment	\$	(11,787)	\$	(16,298)
Goodwill and other intangibles		(81,859)		(112,377)
Total gross deferred tax liabilities		(93,646)		(128,675)
Net deferred tax liabilities	\$	(45,754)	\$	(82,858)

F-16

Table of Contents

In assessing the realizability of deferred tax assets, we consider whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Based on the expectation of future taxable income and that the deductible temporary differences will offset existing taxable temporary differences, we believe it is more likely than not that we will realize the benefits of these deductible differences, net of the existing valuation allowances, at December 31, 2012 and 2011.

Net deferred taxes are recorded both as a current deferred income tax asset and as other long-term liabilities based upon the classification of the related assets and liabilities that give rise to the temporary difference. There are approximately \$39.7 million and \$36.2 million of deferred tax assets related to non-current items that are netted with long-term deferred tax liabilities at December 31, 2012 and 2011, respectively.

Harte-Hanks or one of our subsidiaries files income tax returns in the U.S. federal, U.S. state and foreign jurisdictions. For U.S. federal, U.S. state and foreign returns, we are no longer subject to tax examinations for years prior to 2008.

A reconciliation of the beginning and ending amount of unrecognized tax benefit is as follows:

Balance at January 1, 2011	\$	371
Additions for current year tax positions	\$	0
Additions for prior year tax positions		27
Reductions for prior year tax positions		0
Lapse of statute		(230)
Settlements		(77)
Balance at December 31, 2011	\$	91
Additions for current year tax positions	\$	0
Additions for prior year tax positions		0
Reductions for prior year tax positions		0
Lapse of statute		(40)
Settlements		0
Balance at December 31, 2012	\$	51

Included in the balance as of December 31, 2012 are \$0.1 million of federally effected unrecognized tax benefits that, if recognized, would impact the effective tax rate. We anticipate that it is reasonably possible that we will have a reduction in the liability of up to \$0.1 million during 2013 as a result of lapsing statutes.

We have elected to classify any interest and penalties related to income taxes within income tax expense in our Consolidated Statements of Comprehensive Income (Loss). We recognized \$0.1 million in tax benefits for the reduction of accrued interest and penalties associated with the reduction of the liability for unrecognized tax benefits during each of the years ended December 31, 2012 and 2011. We did not have any interest and penalties accrued at December 31, 2012 or 2011.

As of December 31, 2012, we had net operating loss carryforwards that are available to reduce future taxable income and that will begin to expire in 2026.

Edgar Filing: HARTE HANKS INC - Form 10-K

The valuation allowance for deferred tax assets as of January 1, 2011, was \$3.7 million. The valuation allowance at December 31, 2012 and 2011 relates to foreign and state net operating loss carryforwards, which are not expected to be realized. As part of our assessment of the realizability of our deferred tax assets, and based on the expectations of future taxable income and that the deductible temporary differences will offset existing taxable temporary differences, we reduced our January 1, 2012 valuation allowance associated with the Florida Shoppers net operating loss by \$1.0 million.

F-17

---



Table of Contents

Deferred income taxes have not been provided on the undistributed earnings of our foreign subsidiaries as these earnings have been, and under current plans will continue to be, permanently reinvested in these subsidiaries. As of December 31, 2012, the cumulative undistributed earnings of these subsidiaries were approximately \$4.4 million. If those earnings were not considered permanently reinvested, U.S. federal deferred income taxes would have been recorded, after consideration of U.S. foreign tax credits. However, it is not practicable to estimate the amount of additional taxes which may be payable upon distributions.

Cash payments for income taxes were \$13.6 million, \$15.5 million and \$28.2 million in 2012, 2011 and 2010, respectively.

**Note F Goodwill and Other Intangible Assets**

Goodwill represents the excess of the purchase price of an acquisition over the fair values of the identifiable net assets acquired. Other intangible assets with definite and indefinite useful lives are recorded at fair value at the date of acquisition. The Company tests its goodwill and other intangible assets with indefinite useful lives for impairment as of November 30 of each year and as of an interim date should factors or indicators become apparent that would require an interim test. The company assesses the impairment of its goodwill by determining the fair value of each of its reporting units and comparing the fair value to the carrying value for each reporting unit. We have identified our reporting units as Direct Marketing and Shoppers.

Prior to the sale of our Florida Shoppers in 2012, our Shoppers business operated in regional markets in both California and Florida and was greatly affected by the strength of the state and local economies. Revenues from our Shoppers business were largely dependent on local advertising expenditures in the areas of California and Florida in which we operated. During 2012, the poor economic conditions that we have experienced since the second half of 2007 in California and Florida continued. These conditions were initially created by weakness in the real estate and associated financing markets and have spread and persist across virtually all categories. Management sees little, if any, improvement in the California and Florida economies and the Company expects to have further challenges before performance improves. In response, during the first half of 2012, the Company continued its efforts to reduce expenses in the Shoppers business, primarily through organizational restructuring and the discontinuation of a number of unprofitable digital initiatives, including SaverTime and mobile apps.

As a result of continuing revenue declines in Shoppers, and in conjunction with management's evaluation of the business, the Company determined that a triggering event had occurred and that an interim step-one impairment test of Shoppers' goodwill was warranted in connection with the preparation of its second quarter 2012 financial statements. The fair value of the Shoppers unit was estimated using a discounted cash flow model and a cash flow multiple model, which were consistent with those used in our most recent annual impairment testing as of November 30, 2011. The fair value of our Shoppers unit was estimated to be less than its related carrying value. Management determined that the goodwill balance with respect to this reporting unit was impaired and step-two testing was deemed necessary.

Step-two of the goodwill test consists of performing a hypothetical purchase price allocation, under which the estimated fair value of the reporting unit is allocated to its tangible and intangible assets based on their estimated fair values, with any residual amount being assigned to goodwill. During the step-two analysis, book value was estimated to approximate fair value for all working capital items, as well as a number of insignificant assets and liabilities. Owned real estate and buildings were valued using the market approach and comparable property values. Other significant property, plant and equipment items were valued using the cost approach and trending models to estimate the cost of reproduction and then adjusting for the diminution of value from physical deterioration and obsolescence.

## Edgar Filing: HARTE HANKS INC - Form 10-K

The models used to value the total Shoppers unit in step-one relied heavily on management's assumptions. These assumptions, which are significant to the calculated fair values, are considered Level 3 inputs under the fair value hierarchy established by FASB ASC 820 as they are unobservable. The assumptions in step-one include discount rate, revenue growth rates, tax rates and operating margins. The discount rate represents the expected return on capital of the Shoppers unit. The discount rate was determined using a target structure of 30% debt and 70% equity.

F-18

---

Table of Contents

We used the interest rate of a 30-year government security to determine the risk-free rate in our weighted average cost of capital calculation. Projected growth rates and terminal growth rates are primarily driven by management's best estimate of future performance, giving consideration to historical performance and existing and anticipated economic and competitive conditions. Assumed tax rates represent management's best estimates of blended federal and state income tax rates. Operating margin assumptions are primarily driven by management's best estimate of future performance, giving consideration to historical performance and existing and anticipated economic and competitive conditions.

The impairment analysis indicated that \$156.9 million of goodwill and \$8.4 million of other intangibles, relating to trade names and client relationships associated with the Tampa Flyer (included in the Florida Shoppers operations) acquisition in April 2005, were impaired. As a result, a total impairment charge of \$165.3 million was recorded in the Consolidated Statements of Comprehensive Income (Loss) in the second quarter of 2012. The Company had not previously recorded impairments of either goodwill or other intangible assets. Therefore the amount of impairments recorded in the second quarter of 2012 represents the cumulative amount of goodwill and other intangible asset impairment charges through June 30, 2012.

We performed our annual goodwill impairment testing for both the Direct Marketing and Shoppers segments as of November 30, 2012. Consistent with prior periods, fair value was determined using a discounted cash flow model, a cash flow multiple model, and with consideration of our overall market capitalization. Based on the results of our November 30, 2012 impairment tests, we did not record any additional impairment losses in 2012 related to goodwill. We did not record an impairment loss related to goodwill in 2011 or 2010.

The Company continues to monitor potential triggering events, including changes in the business climate in which it operates, attrition of key personnel, the current volatility in the capital markets, the Company's market capitalization compared to its book value, the Company's recent operating performance, and the Company's financial projections. The occurrence of one or more triggering events could require additional impairment testing, which could result in additional impairment charges in the future.

Excluding the Florida Shoppers operations, which were sold in 2012 and are included in discontinued operations in our Consolidated Financial Statements, the total impairment charge related to our Shoppers business was \$156.9 million, all of which related to goodwill.

The changes in the carrying amount of goodwill are as follows:

In thousands	Direct Marketing	Shoppers	Total
Balance at December 31, 2010	\$ 398,164	\$ 167,487	\$ 565,651
Purchase consideration	0	0	0
Impairment	0	0	0
Balance at December 31, 2011	\$ 398,164	\$ 167,487	\$ 565,651
Purchase consideration	0	0	0
Impairment	0	(156,936)	(156,936)
Balance at December 31, 2012	\$ 398,164	\$ 10,551	\$ 408,715

## Edgar Filing: HARTE HANKS INC - Form 10-K

Other intangibles with indefinite useful lives relate to trade names associated with the Aberdeen acquisition in September 2006. Excluding the Florida Shoppers operations, we did not record an impairment loss related to other intangibles with indefinite lives in any of the years in the three year period ended December 31, 2012. All other intangible asset balances and activity related to the Florida Shoppers operations have been excluded from the following rollforward table.

F-19

---

Edgar Filing: HARTE HANKS INC - Form 10-K

Table of Contents

The changes in the carrying amount of other intangibles with indefinite lives are as follows:

In thousands	Direct Marketing	Shoppers	Total
Balance at December 31, 2010	\$ 5,000	\$ 0	\$ 5,000
Purchase consideration	0	0	0
Impairment	0	0	0
Balance at December 31, 2011	\$ 5,000	\$ 0	\$ 5,000
Purchase consideration	0	0	0
Impairment	0	0	0
Balance at December 31, 2012	\$ 5,000	\$ 0	\$ 5,000

Other intangibles with definite useful lives all relate to contact databases, client relationships and non-compete agreements. Other intangible assets with definite useful lives are amortized on a straight-line basis over their respective estimated useful lives, typically a period of 3 to 10 years, and reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Excluding the Florida Shoppers operations, we did not record an impairment loss related to other intangibles with definite useful lives in any of the years in the three year period ended December 31, 2012. All other intangible asset balances and activity related to the Florida Shoppers operations have been excluded from the following rollforward table.

The changes in the carrying amount of other intangibles with definite lives are as follows:

In thousands	Direct Marketing	Shoppers	Total
Balance at December 31, 2010	\$ 733	\$ 0	\$ 733
Purchase consideration	0	0	0
Amortization	(229)	0	(229)
Impairment	0	0	0
Balance at December 31, 2011	\$ 504	\$ 0	\$ 504
Purchase consideration	0	0	0
Amortization	(245)	0	(245)
Impairment	0	0	0
Balance at December 31, 2012	\$ 259	\$ 0	\$ 259

Amortization expense related to other intangibles with definite useful lives was \$0.2 million, \$0.2 million and \$0.3 million for the years ended December 31, 2012, 2011 and 2010, respectively. Expected amortization expense for the next five years is as follows:

In thousands	
2013	\$ 207
2014	\$ 52
2015	\$ 0
2016	\$ 0

2017 \$ 0

F-20

---

Table of Contents**Note G Employee Benefit Plans**

Prior to January 1, 1999, we maintained a defined benefit pension plan for which most of our employees were eligible. In conjunction with significant enhancements to the 401(k) plan, we elected to freeze benefits under this defined benefit pension plan (frozen pension plan) as of December 31, 1998.

In 1994, we adopted a non-qualified, unfunded, supplemental pension plan (supplemental pension plan) covering certain employees, which provides for incremental pension payments so that total pension payments equal those amounts that would have been payable from the principal pension plan were it not for limitations imposed by income tax regulation. The benefits under this supplemental pension plan will continue to accrue as if the principal pension plan had not been frozen.

The overfunded or underfunded status of our defined benefit postretirement plans is recorded as an asset or liability on our balance sheet. The funded status is measured as the difference between the fair value of plan assets and the projected benefit obligation. Periodic changes in the funded status are recognized through other comprehensive income. We currently measure the funded status of our defined benefit plans as of December 31, the date of our year-end consolidated balance sheets.

The status of the defined benefit pension plans at year-end was as follows:

In thousands	Year Ended December 31,	
	2012	2011
<b>Change in benefit obligation</b>		
Benefit obligation at beginning of year	\$ 160,225	\$ 147,721
Service cost	467	457
Interest cost	7,841	8,118
Actuarial loss	18,745	11,533
Benefits paid	(8,201)	(7,604)
Benefit obligation at end of year	\$ 179,077	\$ 160,225
<b>Change in plan assets</b>		
Fair value of plan assets at beginning of year	\$ 93,002	\$ 97,497
Actual return on plan assets	9,952	(3,185)
Contributions	7,421	6,294
Benefits paid	(8,201)	(7,604)
Fair value of plan assets at end of year	\$ 102,174	\$ 93,002
Funded status at end of year	\$ (76,903)	\$ (67,223)

The following amounts have been recognized in the Consolidated Balance Sheets at December 31:

In thousands	2012	2011
Other current liabilities	\$ 1,437	\$ 1,068

Edgar Filing: HARTE HANKS INC - Form 10-K

Other long-term liabilities		75,466		66,155
	\$	76,903	\$	67,223

The following amounts have been recognized in accumulated other comprehensive loss at December 31:

In thousands		2012		2011
Net loss	\$	54,431	\$	48,702
Prior service cost		0		3
	\$	54,431	\$	48,705

We plan to make total contributions of \$4.6 million to our frozen pension plan in 2013 in order to obtain the Pension Protection Act of 2006 full funding limit exemption.



## Edgar Filing: HARTE HANKS INC - Form 10-K

### Table of Contents

We are not required to make and do not intend to make any contributions to our unfunded, supplemental pension plan in 2013 other than to the extent needed to cover benefit payments. We expect benefit payments under this supplemental pension plan to total \$1.4 million in 2013. In the event of a change of control, as defined in the plan document, this supplemental pension plan is required to be fully funded.

The following information is presented for pension plans with an accumulated benefit obligation in excess of plan assets:

In thousands	December 31,	
	2012	2011
Projected benefit obligation	\$ 179,077	\$ 160,255
Accumulated benefit obligation	\$ 177,442	\$ 158,097
Fair value of plan assets	\$ 102,174	\$ 93,002

The unfunded, supplemental pension plan had an accumulated benefit obligation of \$26.6 million and \$23.5 million at December 31, 2012 and 2011, respectively.

The following table presents the components of net periodic benefit cost and other amounts recognized in other comprehensive loss:

In thousands	Year Ended December 31,		
	2012	2011	2010
<b>Net Periodic Benefit Cost (Pre-tax)</b>			
Service cost	\$ 467	\$ 457	\$ 341
Interest cost	7,841	8,118	7,984
Expected return on plan assets	(6,733)	(7,022)	(6,163)
Amortization of prior service cost	4	49	54
Recognized actuarial loss	5,999	4,519	4,081
Net periodic benefit cost	\$ 7,578	\$ 6,121	\$ 6,297
<b>Amounts Recognized in Other Comprehensive Loss (Pre-tax)</b>			
Net loss	\$ 9,548	\$ 17,222	\$ 2,681
Prior service cost	(4)	(49)	(54)
Total cost recognized in other comprehensive loss	\$ 9,544	\$ 17,173	\$ 2,627
Net cost recognized in net periodic benefit cost and other comprehensive loss	\$ 17,122	\$ 23,294	\$ 8,924

The estimated net loss for the defined benefit pension plans that will be amortized from accumulated other comprehensive loss into net periodic benefit cost in 2013 is \$6.6 million.

The weighted-average assumptions used for measurement of the defined pension plans were as follows:

Edgar Filing: HARTE HANKS INC - Form 10-K

	Year Ended December 31,		
	2012	2011	2010
<b>Weighted-average assumptions used to determine net periodic benefit cost</b>			
Discount rate	5.02%	5.62%	6.20%
Expected return on plan assets	7.25%	7.25%	7.25%
Rate of compensation increase	3.00%	4.00%	4.00%

F-22

---

Edgar Filing: HARTE HANKS INC - Form 10-K

Table of Contents

Weighted-average assumptions used to determine benefit obligations	December 31,	
	2012	2011
Discount rate	4.15%	5.02%
Rate of compensation increase	3.00%	4.00%

The discount rate assumptions are based on current yields of investment-grade corporate long-term bonds. The expected long-term return on plan assets is based on the expected future average annual return for each major asset class within the plan's portfolio (which is principally comprised of equity investments) over a long-term horizon. In determining the expected long-term rate of return on plan assets, we evaluated input from our investment consultants, actuaries, and investment management firms, including their review of asset class return expectations, as well as long-term historical asset class returns. Projected returns by such consultants and economists are based on broad equity and bond indices. Additionally, we considered our historical 15-year compounded returns, which have been in excess of the forward-looking return expectations.

The funded pension plan assets as of December 31, 2012 and 2011, by asset category, are as follows:

In thousands	2012		2011	
	\$	%	\$	%
Equity securities	64,565	63%	59,659	64%
Debt securities	30,881	30%	28,238	30%
Other	6,728	7%	5,105	6%
Total plan assets	\$ 102,174	100%	\$ 93,002	100%

The current economic environment presents employee benefit plans with unprecedented circumstances and challenges, which, in some cases over the last several years, have resulted in large declines in the fair value of investments. The fair values presented have been prepared using values and information available as of December 31, 2012.

The following tables present the fair value measurements of the assets in our funded pension plan:

In thousands	December 31, 2012		December 31, 2011	
	\$	(Level 1)	\$	(Level 1)
Equity securities	64,565	64,565	59,659	59,659
Debt securities	30,881	30,881	28,238	28,238
Other	6,728	6,580	5,105	5,105
Total	\$ 102,174	\$ 102,026	\$ 93,002	\$ 93,002

In thousands	December 31, 2012		December 31, 2011	
	\$	(Level 2)	\$	(Level 2)
Equity securities	0	0	0	0
Debt securities	0	0	0	0
Other	148	148	148	148
Total	\$ 148	\$ 148	\$ 148	\$ 148

Edgar Filing: HARTE HANKS INC - Form 10-K

Equity securities	\$	59,659	\$	59,659	\$	0	\$	0
Debt securities		28,238		28,238		0		0
Other		5,105		5,105		0		0
Total	\$	93,002	\$	93,002	\$	0	\$	0

Assets with estimated fair values measured using Level 2 inputs represent unlisted depository receipts. The fair value of these depository receipts were calculated by our trustee using broker's quotes.

## Edgar Filing: HARTE HANKS INC - Form 10-K

### Table of Contents

The investment policy for the Harte-Hanks, Inc. Pension Plan focuses on the preservation and enhancement of the corpus of the plan's assets through prudent asset allocation, quarterly monitoring and evaluation of investment results, and periodic meetings with investment managers.

The investment policy's goals and objectives are to meet or exceed the representative indices over a full market cycle (3-5 years). The policy establishes the following investment mix, which is intended to subject the principal to an acceptable level of volatility while still meeting the desired return objectives:

	Target	Acceptable Range	Benchmark Index
Domestic Equities	50.0%	35% - 75%	S&P 500
Large Cap Growth	22.5%	15% - 30%	Russell 1000 Growth
Large Cap Value	22.5%	15% - 30%	Russell 1000 Value
Mid Cap Value	5.0%	5% - 15%	Russell Mid Cap Value
Mid Cap Growth	0.0%	0% - 10%	Russell Mid Cap Growth
Domestic Fixed Income	35.0%	15% - 50%	LB Aggregate
International Equities	15.0%	10% - 25%	MSCI EAFE

The funded pension plan provides for investment in various investment types. Investments, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility risk. Due to the level of risk associated with investments, it is reasonably possible that changes in the value of investments will occur in the near term and may impact the funded status of the plan. To address the issue of risk, the investment policy places high priority on the preservation of the value of capital (in real terms) over a market cycle. Investments are made in companies with a minimum five-year operating history and sufficient trading volume to facilitate, under most market conditions, prompt sale without severe market effect. Investments are diversified; reasonable concentration in any one issue, issuer, industry or geographic area is allowed if the potential reward is worth the risk.

The following table presents the investments that represented 5% or more of the funded pension plan's assets as of December 31, 2012 and 2011:

In thousands	2012	%	2011	%
LM Institutional Fund Advisors				
I, Inc. Western Asset Core Plus	\$ 16,793	15%	\$ 15,470	17%
State Street Government STIF 15	\$ 14,419	13%	\$ 5,109	6%
PIMCO Total Return Fund				
Institutional Class	\$ 14,088	13%	\$ 12,765	14%

Investment managers are evaluated by the performance of the representative indices over a full market cycle for each class of assets. The Pension Plan Committee reviews, on a quarterly basis, the investment portfolio of each manager, which includes rates of return, performance comparisons with the most appropriate indices, and comparisons of each manager's performance with a universe of other portfolio managers that employ the same investment style.

The expected future pension benefit payments for the next ten years as of December 31, 2012 are as follows:

Edgar Filing: HARTE HANKS INC - Form 10-K

**In thousands**

2013	\$	8,440
2014		8,695
2015		8,947
2016		9,154
2017		9,371
2018 - 2022		50,576
	\$	95,183

F-24

---

Table of Contents

We also sponsor a 401(k) retirement plan in which we match a portion of employees' voluntary before-tax contributions. Under this plan, both employee and matching contributions vest immediately. Total 401(k) expense recognized in 2012, 2011 and 2010 was \$5.0 million, \$5.2 million and \$5.3 million, respectively.

**Note H Stockholders' Equity**

We paid a quarterly dividend of 8.5 cents per share in each of the first three quarters of 2012 and two dividends of 8.5 cents per share in the fourth quarter of 2012. The second dividend paid in the fourth quarter of 2012 was a one-time acceleration of the regular quarterly dividend we would have ordinarily paid in the first quarter of 2013. As a result, we do not anticipate paying a dividend in the first quarter of 2013. We currently plan to pay a quarterly dividend of 8.5 cents per share in each of the second, third and fourth quarters of 2013, although any actual dividend declaration can be made only upon approval of our Board of Directors, based on its business judgment. We paid a quarterly dividend of 8.0 cents per share in each of the quarters in 2011 and 7.5 cents per share in each of the quarters in 2010.

During 2012, we repurchased 0.7 million shares of our common stock for \$4.4 million under our stock repurchase program that was publicly announced in August 2012. Under this program our Board of Directors has authorized us to spend up to \$10.0 million to repurchase shares of our outstanding common stock. As of December 31, 2012, we had authorization to spend \$5.6 million to repurchase additional shares under this program. From January 1997 through December 2012, we have spent more than \$1.2 billion to repurchase 65.6 million shares under this program and previously announced programs.

During 2012, we received 22,168 shares of our common stock, with an estimated market value of \$0.2 million, in connection with stock option exercises and the vesting of non-vested shares. Since January 1997, we have received 1.9 million shares in connection with stock option exercises and the vesting of non-vested shares.

**Note I Stock-Based Compensation**

Compensation expense for stock-based awards is based on the fair values of the awards on the date of grant and is recognized on a straight-line basis over the vesting period of the entire award in the Labor line of the Consolidated Statements of Comprehensive Income (Loss). For the years ended December 31, 2012, 2011 and 2010, we recorded total stock-based compensation expense of \$3.4 million, \$5.0 million and \$3.9 million, respectively. \$0.5 million of the 2011 stock-based compensation related to the retirement of the President of Harte-Hanks Shoppers. In connection with his retirement on August 31, 2011, all of his unvested stock-based awards vested.

In May 2005, we adopted the 2005 Omnibus Incentive Plan (2005 Plan), a stockholder approved plan, pursuant to which we may issue equity securities to directors, officers and key employees. Under the 2005 Plan we have awarded stock options, non-vested shares and performance stock units. The 2005 Plan replaced the 1991 Stock Option Plan (1991 Plan), a stockholder approved plan, pursuant to which we issued stock options to directors, officers and key employees. No additional options will be granted under the 1991 Plan. As of December 31, 2012, there were 3.6 million shares available for grant under the 2005 Plan.

Stock Options

Under the 2005 Plan, all options have been granted at exercise prices equal to the market value of the common stock on the grant date (2005 Plan options). All 2005 Plan options granted prior to 2011 become exercisable in 25% increments on the second, third, fourth and fifth anniversaries of their date of grant and expire on the tenth anniversary of their date of grant. All options granted in 2011 and 2012 become exercisable in 25% increments on the first, second, third and fourth anniversaries of their date of grant, and expire on the tenth anniversary of their date of grant. As of December 31, 2012, 2005 Plan options to purchase 4.1 million shares were outstanding with exercise prices ranging from \$6.04 to \$28.85 per share.

Under the 1991 Plan, options were granted at exercise prices equal to the market value of the common stock on the grant date (1991 Plan market price options) and at exercise prices below the market value of the common stock (1991 Plan performance options). 1991 Plan market price options become exercisable in 25% increments on the second, third, fourth and fifth anniversaries of their date of grant and expire on the tenth anniversary of their date of grant. As



## Edgar Filing: HARTE HANKS INC - Form 10-K

### Table of Contents

of December 31, 2012, 1991 Plan market price options to purchase 1.0 million shares were outstanding with exercise prices ranging from \$17.45 to \$25.63 per share. No 1991 Plan performance options have been granted since January 1999, and all remaining 1991 Plan performance options were exercised in January 2009.

All options granted under the 1991 Plan and 2005 Plan vest in full upon a change of control (as defined in each plan).

The following summarizes all stock option activity during the years ended December 31, 2012, 2011 and 2010:

	Number of Shares	Weighted- Average Option Price	Weighted- Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (Thousands)
Options outstanding at December 31, 2009	6,995,649	\$ 16.63		
Granted	1,514,500	11.89		
Exercised	(5,550)	13.64		\$ 7
Unvested options forfeited	(282,196)	12.60		
Vested options expired	(649,393)	16.50		
Options outstanding at December 31, 2010	7,573,010	\$ 15.85		
Granted	420,500	11.68		
Exercised	(118,250)	6.04		\$ 717
Unvested options forfeited	(363,192)	11.17		
Vested options expired	(758,440)	18.16		
Options outstanding at December 31, 2011	6,753,628	\$ 15.75		
Granted	970,500	8.98		
Exercised	(106,375)	6.04		\$ 297
Unvested options forfeited	(798,311)	10.28		
Vested options expired	(1,712,813)	19.33		
Options outstanding at December 31, 2012	5,106,629	\$ 14.32	5.51	\$ 0
Exercisable at December 31, 2012	2,850,335	\$ 18.06	3.69	\$ 0

The aggregate intrinsic value at year end in the table above represents the total pre-tax intrinsic value that would have been received by the option holders if all of the in-the-money options were exercised on December 31, 2012. The pre-tax intrinsic value is the difference between the closing price of our common stock on December 31, 2012 and the exercise price for each in-the-money option. This value fluctuates with the changes in the price of our common stock. The intrinsic value is zero at December 31, 2012 as the exercise prices of all outstanding options are above the closing price of our common stock.

## Edgar Filing: HARTE HANKS INC - Form 10-K

### Table of Contents

The following table summarizes information about stock options outstanding at December 31, 2012:

Range of Exercise Prices	Number Outstanding	Outstanding		Exercisable	
		Weighted-Average Exercise Price	Weighted-Average Remaining Life (Years)	Number Exercisable	Weighted-Average Exercise Price
\$ 0.00 - 6.99	1,008,750	\$ 6.04	5.90	535,250	\$ 6.04
\$ 7.00 - 10.99	933,000	\$ 8.81	9.30	15,000	\$ 7.86
\$ 11.00 - 11.99	860,625	\$ 11.90	6.90	291,125	\$ 11.90
\$ 12.00 - 15.99	684,626	\$ 14.36	6.03	389,332	\$ 15.16
\$ 16.00 - 24.49	657,216	\$ 21.10	1.35	657,216	\$ 21.10
\$ 24.50 - 28.85	962,412	\$ 25.87	2.64	962,412	\$ 25.87
	5,106,629	\$ 14.32	5.51	2,850,335	\$ 18.06

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model based on the following weighted-average assumptions used for grants during 2012, 2011 and 2010:

	Years Ended December 31,		
	2012	2011	2010
Expected term (in years)	6.25	6.25	6.75
Expected stock price volatility	44.24%	39.76%	36.03%
Risk-free interest rate	1.05%	2.43%	2.70%
Expected dividend yield	3.41%	2.42%	2.42%

Expected term is estimated using the simplified method, which takes into account vesting and contractual term. The simplified method is being used to calculate expected term instead of historical experience due to a lack of relevant historical data resulting from changes in option vesting schedules and changes in the pool of employees receiving option grants. Expected stock price volatility is based on the historical volatility from traded shares of our stock over the expected term. The risk-free interest rate is based on the rate of a zero-coupon U.S. Treasury instrument with a remaining term approximately equal to the expected term. Expected dividend yield is based on historical stock price movement and anticipated future annual dividends over the expected term. Future annual dividends over the expected term are estimated to range between \$0.34 and \$0.44 per share, with a weighted-average annual dividend of \$0.39 per share.

The weighted-average fair value of options granted during 2012, 2011 and 2010 was \$2.74, \$3.85 and \$3.70, respectively. As of December 31, 2012, there was \$4.3 million of total unrecognized compensation cost related to unvested stock options. This cost is expected to be recognized over a weighted average period of approximately 2.56 years.

### Non-vested Shares

All non-vested shares have been granted under the 2005 Plan. In general, all non-vested shares granted prior to 2011 vest 100% on the third anniversary of their date of grant. The majority of non-vested shares granted in 2011 and 2012 vest in three equal increments on the first, second and third anniversaries of their date of grant. The remaining non-vested shares granted in 2011 and 2012 vest 100% on the third anniversary of their date of grant. Non-vested shares granted under the 2005 Plan also vest upon a change of control.



Table of Contents

The following summarizes all non-vested share activity during 2012, 2011 and 2010:

	Number of Shares		Weighted- Average Grant-Date Fair Value
Non-vested shares outstanding at December 31, 2009	153,740	\$	15.76
Granted	85,747		11.93
Vested	(48,201)		24.79
Forfeited	(10,000)		24.86
Non-vested shares outstanding at December 31, 2010	181,286	\$	11.05
Granted	300,224		12.31
Vested	(53,671)		15.04
Forfeited	(8,499)		11.95
Non-vested shares outstanding at December 31, 2011	419,340	\$	11.42
Granted	332,113		9.91
Vested	(143,626)		9.82
Forfeited	(107,374)		11.09
Non-vested shares outstanding at December 31, 2012	500,453	\$	10.95

The fair value of each non-vested share is estimated on the date of grant as the closing market price of our common stock on the date of grant. As of December 31, 2012, there was \$3.0 million of total unrecognized compensation cost related to non-vested shares. This cost is expected to be recognized over a weighted average period of approximately 1.71 years.

Performance Stock Units

All performance stock units have been granted under the 2005 Plan. Performance stock units are a form of share-based awards similar to non-vested shares, except that the number of shares ultimately issued is based on our performance against specific performance goals over a three-year period. At the end of the performance period, the number of shares of stock issued will be determined by adjusting upward or downward from the maximum in a range between 0% and 100%. Upon a change of control, outstanding performance stock units will be paid out at the 100% level.

Table of Contents

The following summarizes all performance stock unit activity during 2012, 2011 and 2010:

	Number of Shares		Weighted- Average Grant-Date Fair Value
Performance stock units outstanding at December 31, 2009	57,450	\$	20.52
Granted	0		0
Issued	0		0
Forfeited	(33,200)		24.56
Performance stock units outstanding at December 31, 2010	24,250	\$	14.98
Granted	188,800		11.34
Issued	(19,200)		11.34
Forfeited	(24,250)		14.98
Performance stock units outstanding at December 31, 2011	169,600	\$	11.34
Granted	136,000		8.84
Issued	0		0
Forfeited	(65,900)		10.15
Performance stock units outstanding at December 31, 2012	239,700	\$	10.25

The fair value of each performance stock unit is estimated on the date of grant as the closing market price of our common stock on the date of grant, minus the present value of anticipated dividend payments. Periodic compensation expense is based on the current estimate of future performance against specific performance goals over a three-year period and is adjusted up or down based on those estimates.

**Note J Commitments and Contingencies**

At December 31, 2012, we had letters of credit in the amount of \$9.9 million, \$9.5 of which were issued under the 2010 Revolving Credit Facility. No amounts were drawn against these letters of credit at December 31, 2012. These letters of credit exist to support insurance programs relating to workers' compensation, automobile and general liability, as well as a real estate obligation.

On January 25, 2010, Harte-Hanks Shoppers, Inc. (Shoppers), a California corporation and a subsidiary of Harte-Hanks, Inc. (Harte-Hanks), reached an agreement in principle with Shoppers employee Frank Gattuso and former employee Ernest Sigala, individually and on behalf of a certified class, to settle and resolve a previously disclosed class action lawsuit filed in 2001 (*Frank Gattuso et al. v. Harte-Hanks Inc. et al.*, as further described below). During the fourth quarter of 2009 we accrued the full \$7.0 million associated with this agreement. This agreement in principle was reduced to a class settlement agreement executed by the parties, and received final approval from the court on May 26, 2011. Pursuant to the settlement agreement, Shoppers established a class settlement fund of \$7.0 million. In return, each member of the class, including Gattuso and Sigala, released all claims against Shoppers and its affiliates that in any way arose from or related to the matters which were the subject of, or could have been the subject of, the claims alleged in the class action lawsuit. Payments under the class settlement agreement from the class settlement fund concluded in August 2011, and at that time \$1.3 million of unclaimed funds reverted back to Shoppers.

## Edgar Filing: HARTE HANKS INC - Form 10-K

In the normal course of our business, we are obligated under some agreements to indemnify our clients as a result of claims that we infringe on the proprietary rights of third parties. The terms and duration of these commitments vary and, in some cases, may be indefinite, and certain of these commitments do not limit the maximum amount of future

F-29

---

Table of Contents

payments we could become obligated to make there under; accordingly, our actual aggregate maximum exposure related to these types of commitments cannot be reasonably estimated. Historically, we have not been obligated to make significant payments for obligations of this nature, and no liabilities have been recorded for these obligations in our financial statements.

We are also currently subject to various other legal proceedings in the course of conducting our businesses and, from time to time, we may become involved in additional claims and lawsuits incidental to our businesses. In the opinion of management, after consultation with counsel, none of these matters is currently considered to be reasonably possible of resulting in a material adverse effect on our consolidated financial position or results of operations. Nevertheless, we cannot predict the impact of future developments affecting our pending or future claims and lawsuits and any resolution of a claim or lawsuit within a particular fiscal quarter may adversely impact our results of operations for that quarter. We expense legal costs as incurred, and all recorded legal liabilities are adjusted as required as better information becomes available to us. The factors we consider when recording an accrual for contingencies include, among others: (i) the opinions and views of our legal counsel; (ii) our previous experience; and (iii) the decision of our management as to how we intend to respond to the complaints.

**Note K Leases**

We lease certain real estate and equipment under numerous lease agreements, most of which contain some renewal options. The total rent expense applicable to operating leases was \$17.6 million, \$21.0 million and \$23.0 million for the years ended December 31, 2012, 2011 and 2010, respectively.

Step rent provisions and escalation clauses, capital improvement funding, rent holidays and other lease concessions are taken into account in computing minimum lease payments. We recognize the minimum lease payments on a straight-line basis over the minimum lease term.

The future minimum rental commitments for all non-cancelable operating leases with terms in excess of one year as of December 31, 2012 are as follows:

<b>In thousands</b>	
2013	\$ 15,689
2014	12,762
2015	7,884
2016	5,510
2017	3,937
After 2017	3,491
	\$ 49,273

We also lease certain equipment and software under capital leases. Our capital lease obligations at year-end were as follows:

<b>In thousands</b>	<b>December 31,</b>	
	<b>2012</b>	<b>2011</b>

Edgar Filing: HARTE HANKS INC - Form 10-K

Current portion of capital leases	\$	369	\$	402
Long-term portion of capital leases		302		305
Total capital lease obligations	\$	671	\$	707

F-30

---



# Edgar Filing: HARTE HANKS INC - Form 10-K

## Table of Contents

The future minimum lease payments for all capital leases operating as of December 31, 2012 are as follows:

<b>In thousands</b>		
2013	\$	369
2014		212
2015		73
2016		16
2017		1
After 2017		0
	\$	671

## **Note L Earnings Per Share**

Basic earnings per share is computed on the basis of the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed on the basis of the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares include outstanding stock options and non-vested shares.

Reconciliations of basic and diluted earnings per share (EPS) are as follows:

<b>In thousands, except per share amounts</b>	<b>Year Ended December 31,</b>		
	<b>2012</b>	<b>2011</b>	<b>2010</b>
<b>Net Income</b>			
Income (loss) from continuing operations	\$ (73,104)	\$ 45,877	\$ 55,194
Loss from discontinued operations	(10,249)	(1,679)	(1,590)
Net income (loss)	(83,353)	44,198	53,604
<b>Basic EPS</b>			
Weighted-average common shares outstanding used in earnings per share computations	62,887	63,173	63,616
<b>Basic earnings (loss) per share</b>			
Continuing operations	\$ (1.16)	\$ 0.73	\$ 0.87
Discontinued operations	(0.17)	(0.03)	(0.03)
Net Income	\$ (1.33)	\$ 0.70	\$ 0.84
<b>Diluted EPS</b>			
Shares used in diluted earnings per share computations	62,887	63,552	64,139
<b>Diluted earnings (loss) per share</b>			
Continuing operations	\$ (1.16)	\$ 0.72	\$ 0.86
Discontinued operations	(0.17)	(0.02)	(0.02)
Net Income	\$ (1.33)	\$ 0.70	\$ 0.84

**Computation of Shares Used in Earnings Per Share Computations**

Weighted-average common shares outstanding	62,887	63,173	63,616
Weighted-average common equivalent shares dilutive effect of stock options and awards	0	379	523
Shares used in diluted earnings per share computations	62,887	63,552	64,139

There are no dilutive shares for the year ended December 31, 2012 as the Company has a net loss for the period. All 6.1 million weighted-average outstanding market price options and 0.6 million weighted-average outstanding non-vested shares have been excluded from the calculation of shares used in the diluted EPS calculation as they are considered anti-dilutive.

5.4 million and 6.0 million weighted-average anti-dilutive options have been excluded from the EPS calculations for the years ended December 31, 2011 and 2010, respectively. There were no anti-dilutive non-vested shares for the years ended December 31, 2011 and 2010, respectively.

Table of Contents**Note M Comprehensive Income**

Comprehensive income for a period encompasses net income and all other changes in equity other than from transactions with our stockholders. Our comprehensive income was as follows:

In thousands	Year Ended December 31,		
	2012	2011	2010
Net income (loss)	\$ (83,353)	\$ 44,198	\$ 53,604
Other comprehensive income (loss):			
Adjustment to pension liability	(9,544)	(17,173)	(2,627)
Tax benefit	3,818	6,869	1,051
Adjustment to pension liability, net of tax	(5,726)	(10,304)	(1,576)
Foreign currency translation adjustment	1,315	(1,337)	(136)
Total other comprehensive loss	(4,411)	(11,641)	(1,712)
Total comprehensive income (loss)	\$ (87,764)	\$ 32,557	\$ 51,892

**Note N Selected Quarterly Data (Unaudited)**

In thousands, except per share amounts	2012 Quarter Ended				2011 Quarter Ended			
	December 31	September 30	June 30	March 31	December 31	September 30	June 30	March 31
Revenues	\$ 204,835	\$ 187,203	\$ 189,629	\$ 186,042	\$ 215,113	\$ 202,967	\$ 202,838	\$ 190,718
Operating income (loss)	22,142	17,345	(143,403)	13,976	24,622	21,178	17,234	15,064
Income (loss) from continuing operations	14,343	9,756	(104,638)	7,435	15,310	12,263	9,954	8,350
Loss from discontinued operations	(3,647)	(893)	(5,067)	(642)	(582)	(135)	(529)	(433)
Net income (loss)	10,696	8,863	(109,705)	6,793	14,728	12,128	9,425	7,917
Basic earnings (loss) per share:								
Continuing operations	\$ 0.23	\$ 0.15	\$ (1.66)	\$ 0.12	\$ 0.24	\$ 0.20	\$ 0.16	\$ 0.13
Discontinued operations	(0.06)	(0.01)	(0.08)	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)
Net income (loss)	0.17	0.14	(1.74)	0.11	0.23	0.19	0.15	0.12
Diluted earnings (loss) per share:								
Continuing operations	\$ 0.23	\$ 0.15	\$ (1.66)	\$ 0.12	\$ 0.24	\$ 0.19	\$ 0.16	\$ 0.13
Discontinued operations	(0.06)	(0.01)	(0.08)	(0.01)	(0.01)	(0.00)	(0.01)	(0.01)
Net income (loss)	0.17	0.14	(1.74)	0.11	0.23	0.19	0.15	0.12

Earnings per common share amounts are computed independently for each of the quarters presented. Therefore, the sum of the quarterly earnings per share amounts may not equal the quarterly net income earnings per share amounts or the annual earnings per share amounts.

**Note O Business Segments**

## Edgar Filing: HARTE HANKS INC - Form 10-K

Harte-Hanks is a worldwide direct and targeted marketing company with operations in two segments Direct Marketing and Shoppers.

Harte-Hanks Direct Marketing uses various capabilities and technologies to enable our clients to capture, analyze and disseminate customer and prospect data across all points of customer contact. Direct Marketing services are targeted to specific industries or markets with services and software products tailored to each industry or market. Currently, our Direct Marketing business services various vertical markets including retail, high-tech/telecom, financial services,

F-32

---

Table of Contents

pharmaceutical/healthcare, and a wide range of selected markets. We believe that we are generally able to provide services to new industries and markets by modifying our services and applications as opportunities are presented. Depending on the needs of our clients, our Direct Marketing capabilities are provided in an integrated approach through more than 30 facilities worldwide, more than 10 of which are located outside of the United States. Each of these centers possesses some specialization and is linked with others to support the needs of our clients.

Harte-Hanks Shoppers is North America's largest owner, operator and distributor of shopper publications, based on weekly circulation and revenues. Shoppers are weekly advertising publications delivered free by Standard Mail to households and businesses in a particular geographic area. Shoppers offer advertisers a targeted, cost-effective local advertising system, with virtually 100% penetration in their area of distribution. Shoppers are particularly effective in large markets with high media fragmentation in which major metropolitan newspapers generally have low penetration. Our Shoppers segment also provides online advertising and other services online through our website, *PennySaverUSA.com*. Our Shoppers clients range from large national companies to local neighborhood businesses to individuals with a single item for sale. The segment's core clients are local service businesses and small retailers. Shoppers' client base is entirely domestic.

On December 31, 2012 we sold the assets of our Florida Shoppers operations, The Flyer®, for gross proceeds of \$2.0 million in the form of a secured promissory note, subject to working capital adjustments. This transaction resulted in an after-tax loss of \$2.7 million, including reserving the full amount of the promissory note. After this sale, Harte-Hanks Shoppers no longer has any operations or circulation in the state of Florida. At December 31, 2012, our Shoppers publications were zoned into approximately 780 separate editions with total circulation of approximately 9.1 million shopper packages in California each week.

Included in Corporate Activities are general corporate expenses. Assets of Corporate Activities primarily include unallocated cash, investments and deferred income taxes.

Information about our operations in different business segments is set forth below based on the nature of the products and services offered. We evaluate performance based on several factors, of which the primary financial measures are segment revenues and operating income. The accounting policies of the business segments are the same as those described in Note A, *Significant Accounting Policies*.

Edgar Filing: HARTE HANKS INC - Form 10-K

Table of Contents

In thousands	Year Ended December 31,		
	2012	2011	2010
<b>Revenues</b>			
Direct Marketing	\$ 581,091	\$ 614,270	\$ 601,283
Shoppers	186,618	197,366	219,437
Total revenues	\$ 767,709	\$ 811,636	\$ 820,720
<b>Operating income (loss)</b>			
Direct Marketing	\$ 75,398	\$ 83,490	\$ 86,748
Shoppers	(152,610)	5,839	17,795
Corporate Activities	(12,728)	(11,231)	(11,297)
Total operating income (loss)	\$ (89,940)	\$ 78,098	\$ 93,246
<b>Income (loss) from continuing operations before income taxes</b>			
Operating income (loss)	\$ (89,940)	\$ 78,098	\$ 93,246
Interest expense	(3,574)	(3,184)	(2,824)
Interest income	91	249	200
Other, net	(2,863)	1,505	(2,136)
Income (loss) from continuing operations before income taxes	\$ (96,286)	\$ 76,668	\$ 88,486
<b>Depreciation</b>			
Direct Marketing	\$ 15,659	\$ 15,195	\$ 16,792
Shoppers	4,498	4,409	4,638
Corporate Activities	19	18	13
Total depreciation	\$ 20,176	\$ 19,622	\$ 21,443
<b>Other intangible amortization</b>			
Direct Marketing	\$ 245	\$ 229	\$ 290
Shoppers	0	0	0
Total intangible amortization	\$ 245	\$ 229	\$ 290
<b>Capital expenditures</b>			
Direct Marketing	\$ 13,461	\$ 19,378	\$ 15,992
Shoppers	395	1,580	1,140
Corporate Activities	0	12	69
Total capital expenditures	\$ 13,856	\$ 20,970	\$ 17,201

In thousands	December 31,	
	2012	2011
<b>Total assets</b>		
Direct Marketing	\$ 609,673	\$ 674,776
Shoppers	49,001	153,679
Corporate Activities	47,538	87,870
Total assets	\$ 706,212	\$ 916,325

Table of Contents

Information about the operations in different geographic areas:

In thousands	Year Ended December 31,		
	2012	2011	2010
<b>Revenues (a)</b>			
United States	\$ 678,736	\$ 720,747	\$ 728,205
Other countries	88,973	90,889	92,515
Total revenues	\$ 767,709	\$ 811,636	\$ 820,720

In thousands	December 31,	
	2012	2011
<b>Property, plant and equipment (b)</b>		
United States	\$ 55,467	\$ 62,538
Other countries	6,504	6,354
Total property, plant and equipment	\$ 61,971	\$ 68,892

(a) Geographic revenues are based on the location of the service being performed.

(b) Property, plant and equipment are based on physical location.

**Note P Discontinued Operations**

We sold the assets of our Florida Shoppers operations to Coda Media Corp. on December 31, 2012 for gross proceeds of approximately \$2.0 million in the form of a secured promissory note, subject to working capital adjustments. This transaction resulted in a loss on the sale of \$2.7 million, net of \$2.1 million of income tax benefit. The promissory note, which is secured by the assets which were sold, includes an interest rate of 2.5% per annum and is structured to make payments of interest only in each of the first three quarters of 2013, and a payment of total principal and unpaid interest on December 31, 2013. Due to a number of factors that put the collectability of the note in doubt, we have fully reserved the amount of this note receivable. These factors include the lack of cash paid at the date of the sale, the structure and length of the note, and historical and projected cash flows from the sold operations. This reserve was included in the calculation of the loss on the sale.

Because the Florida Shoppers represent a distinct business unit with operations and cash flows that can clearly be distinguished, both operationally and for financial purposes, from the rest of Harte-Hanks, Inc., the results of the Florida Shoppers operations are reported as discontinued operations for all periods presented. Results of the remaining Harte-Hanks, Inc. business segments are reported as continuing operations.

Summarized operating results for the Florida Shoppers discontinued operations are as follows:

In thousands	Year Ended December 31,		
	2012	2011	2010

Edgar Filing: HARTE HANKS INC - Form 10-K

Revenues	\$	36,118	\$	39,129	\$	39,806
Loss from discontinued operations before impairment charges and income taxes		(4,114)		(2,696)		(2,159)
Impairment of other intangible assets before income taxes		(8,400)		0		0
Loss on sale before income taxes		(4,863)		0		0
Income tax benefit		7,128		1,017		569
Loss from discontinued operations	\$	(10,249)	\$	(1,679)	\$	(1,590)

F-35

---



Table of Contents

Summarized balance sheet data for the Florida Shoppers discontinued operations are as follows:

<b>In thousands</b>	<b>December 31,</b>	
	<b>2012</b>	<b>2011</b>
Current assets	\$ 0	\$ 3,879
Property, plant and equipment	0	2,691
Other intangible assets	0	9,484
Other assets	0	134
<b>Total assets</b>	<b>0</b>	<b>16,188</b>
Current liabilities	0	(1,420)
Other liabilities	0	(21)
<b>Total liabilities</b>	<b>0</b>	<b>(1,441)</b>
<b>Net assets of discontinued operations</b>	<b>\$ 0</b>	<b>\$ 14,747</b>

The major components of cash flows for the Florida Shoppers discontinued operations are as follows:

<b>In thousands</b>	<b>Year Ended December 31,</b>		
	<b>2012</b>	<b>2011</b>	<b>2010</b>
Loss from discontinued operations	\$ (10,249)	\$ (1,679)	\$ (1,590)
Impairment of goodwill and other intangible assets	8,400	0	0
Loss on sale	4,863	0	0
Depreciation and software amortization	563	789	994
Intangible asset amortization	386	572	700
Other, net	513	(724)	855
<b>Net cash provided by (used in) discontinued operations</b>	<b>\$ 4,476</b>	<b>\$ (1,042)</b>	<b>\$ 959</b>

Table of Contents

**INDEX TO EXHIBITS**

We are incorporating certain exhibits listed below by reference to other Harte-Hanks filings with the Securities and Exchange Commission, which we have identified in parentheses after each applicable exhibit.

<b>Exhibit No.</b>	<b>Description of Exhibit</b>
<b>Charter Documents</b>	
3(a)	Amended and Restated Certificate of Incorporation as amended through May 5, 1998 (filed as Exhibit 3(e) to the Company's Form 10-Q for the six months ended June 30, 1998).
3(b)	Third Amended and Restated Bylaws (filed as Exhibit 3.1 to the Company's Form 8-K dated December 6, 2010).
<b>Credit Agreements</b>	
10.1(a)	Term Loan Agreement by and between Harte-Hanks, Inc. and Wells Fargo Bank, N.A. as administrative agent, dated March 7, 2008 (filed as Exhibit 10.1 to the Company's Form 8-K dated March 7, 2008).
10.1(b)	Revolving Credit Agreement dated as of August 12, 2010 between Harte-Hanks, Inc., each lender from time to time party hereto, and Bank of America, N. A., as Administrative Agent (filed as Exhibit 10.1 to the Company's Form 8-K, dated August 12, 2010).
10.1(c)	First Amendment to Term Loan Agreement dated as of August 12, 2010 between Harte-Hanks, Inc., and Wells Fargo Bank, N. A., as Administrative Agent (filed as Exhibit 10.2 to the Company's Form 8-K, dated August 12, 2010).
10.1(d)	Term Loan Agreement dated as of August 16, 2011 between Harte-Hanks, Inc., each lender from time to time party thereto, and Bank of America, N. A., as administrative agent (filed as Exhibit 10.1 to the Company's Form 8-K, dated August 16, 2011).
10.1(e)	First Amendment to Revolving Credit Agreement dated as of August 16, 2011 Between Harte-Hanks, Inc., each lender from time to time party thereto, and Bank of America, N. A., as administrative agent (filed as Exhibit 10.2 to the Company's Form 8-K, dated August 16, 2011).
10.1(f)	Second Amendment to Term Loan Agreement dated as of August 16, 2011 Between Harte-Hanks, Inc., each lender from time to time party thereto and Wells Fargo Bank, N.A., as administrative agent (filed as Exhibit 10.3 to the Company's Form 8-K, dated August 16, 2011).
<b>Management and Director Compensatory Plans and Forms of Award Agreements</b>	
10.2(a)	Harte-Hanks, Inc. Restoration Pension Plan (As Amended and Restated Effective January 1, 2008) (filed as Exhibit 10.1 to the Company's Form 8-K dated June 27, 2008).



## Edgar Filing: HARTE HANKS INC - Form 10-K

### Table of Contents

10.2(b)	Harte-Hanks, Inc. Deferred Compensation Plan (As Amended and Restated Effective January 1, 2008) (filed as Exhibit 10.3 to the Company's Form 10-K dated June 27, 2008).
10.2(c)	Harte-Hanks Communications, Inc. 1996 Incentive Compensation Plan (filed as Exhibit 10(p) to the Company's Form 10-Q for the six months ended June 30, 1996).
10.2(d)	Harte-Hanks, Inc. Amended and Restated 1991 Stock Option Plan (filed as Exhibit 10(g) to the Company's Form 10-Q for the six months ended June 30, 1998).
10.2(e)	Form of Non Qualified Stock Option Agreement for employees granted under the Amended and Restated 1991 Stock Option Plan (filed as Exhibit 10(i) to the Company's Form 10-K for the year ended December 31, 2005).
10.2(f)	Form of Non Qualified Stock Option Agreement for directors granted Under the Amended and Restated 1991 Stock Option Plan (filed as Exhibit 10(j) to the Company's Form 10-K for the year ended December 31, 2005).
10.2(g)	Harte-Hanks, Inc. 2005 Omnibus Incentive Plan (As Amended and Restated Effective February 13, 2009) (filed as Exhibit 10.1 to the Company's Form 8-K dated February 13, 2009).
10.2(h)	Amendment to Harte-Hanks, Inc. 2005 Omnibus Incentive Plan, dated as of May 12, 2009 (incorporated by reference to Exhibit 4.4 to Harte-Hanks Registration Statement on Form S-8, filed on May 12, 2009).
10.2(i)	Form of 2005 Omnibus Incentive Plan Non-Qualified Stock Option Agreement (filed as Exhibit 10.2(i) to the Company's Form 10-K dated March 7, 2012).
10.2(j)	Form of 2005 Omnibus Incentive Plan Bonus Stock Agreement (filed as Exhibit 10.2(j) to the Company's Form 10-K dated March 7, 2012).
10.2(k)	Form of 2005 Omnibus Incentive Plan Restricted Stock Award Agreement (filed as Exhibit 10.2(k) to the Company's Form 10-K dated March 7, 2012).
10.2(l)	Form of 2005 Omnibus Incentive Plan Performance Unit Award Agreement (filed as Exhibit 10.2(l) to the Company's Form 10-K dated March 7, 2012).
10.2(m)	Summary of Non-Employee Directors' Compensation (filed as Exhibit 10.1(q) to the Company's Form 10-K for the fiscal year ended December 31, 2008).

### **Executive Officer Employment and Separation Agreements**

10.3(a)	Transition and Consulting Agreement, dated as of August 29, 2007, by and between the Company and Richard Hochhauser (filed as Exhibit 10.1 to the Company's Form 8-K dated August 29, 2007).
---------	--

---

Table of Contents

10.3(b)	Form of Change of Control Severance Agreement between the Company and its Corporate Officers (filed as Exhibit 10.1 to the Company's Form 8-K, dated March 15, 2011).
10.3(c)	Form of Employment Restrictions Agreement signed by the Corporate Officers of the Company (filed as Exhibit 10.3 to the Company's Form 8-K dated March 15, 2011).
10.3(d)	Transition Agreement, dated as of December 15, 2008, by and between the Company and Dean Blythe (filed as Exhibit 10.1 to the Company's Form 8-K dated December 15, 2008).
10.3 (e)	Transition and Consulting Agreement, dated as of July 25, 2011, Between the Company and Peter E. Gorman (filed as Exhibit 10.1 to the Company's Form 8-K dated July 26, 2011).

**Other Exhibits**

*21	Subsidiaries of the Company.
*23	Consent of KPMG LLP, Independent Registered Public Accounting Firm.
*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	Furnished Certification of Chief Executive Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
*32.2	Furnished Certification of 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, as applicable

---