VERIFONE SYSTEMS, INC.
Form 10-Q
September 10, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q
(Mark One)

þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended July 31, 2012

Or

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission file number: 001-32465

VERIFONE SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

Delaware	04-3692546
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2099 Gateway Place, Suite 600
San Jose, CA 95110
(Address of principal executive offices with zip code)
(408) 232-7800
(Registrant's telephone number, including area code)
N/A
(Former name, former address and former fiscal year, if changed since last report)

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 þ No ¨

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

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

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

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

At August 31, 2012, the number of shares outstanding of the registrant's common stock, $0.01 par value was 107,811,832.

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PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (Unaudited)

VERIFONE SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2012	2011	2012	2011
	(Unaudited)			
	(In thousands, except per share data)			
Net revenues:				
System solutions	$350,230	$253,659	$1,003,314	$714,700
Services	138,820	63,292	377,278	178,462
Total net revenues	489,050	316,951	1,380,592	893,162
Cost of net revenues:				
System solutions	206,213	150,621	607,238	428,357
Services	75,330	34,718	217,050	99,117
Total cost of net revenues	281,543	185,339	824,288	527,474
Gross margin	207,507	131,612	556,304	365,688
Operating expenses:				
Research and development	38,657	27,457	111,585	74,501
Sales and marketing	46,182	32,769	132,309	92,214
General and administrative	43,414	28,657	138,148	79,716
Patent litigation loss contingency expense	—	—	17,632	—
Amortization of purchased intangible assets	23,177	1,980	60,549	5,959
Total operating expenses	151,430	90,863	460,223	252,390
Operating income	56,077	40,749	96,081	113,298
Interest expense	(16,374)	(7,963)	(49,644)	(22,998)
Interest income	1,110	479	3,260	1,049
Other income (expense), net	(721)	6,313	(23,350)	6,152
Income before income taxes	40,092	39,578	26,347	97,501
Provision for (benefit from) income taxes	2,313	13,072	(12,068)	13,702
Consolidated net income	37,779	26,506	38,415	83,799
Net income attributable to noncontrolling interests	(84)	(159)	(366)	(221)
Net income attributable to VeriFone Systems, Inc. stockholders	$37,695	$26,347	$38,049	$83,578
Net income per share attributable to VeriFone Systems, Inc. stockholders:				
Basic	$0.35	$0.29	$0.36	$0.95
Diluted	$0.34	$0.28	$0.34	$0.90
Weighted average shares used in computing earnings per share:				

Basic	107,568	89,602	106,768	88,368
Diluted	110,384	93,322	110,305	92,690

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

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VERIFONE SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	July 31, 2012	October 31, 2011
	(Unaudited)	
	(In thousands, except par value)	
ASSETS		
Current assets:		
Cash and cash equivalents	$409,807	$594,562
Accounts receivable, net of allowance of $6,585 and $5,658	371,170	294,440
Inventories	164,873	144,316
Prepaid expenses and other current assets	153,167	127,130
Total current assets	1,099,017	1,160,448
Fixed assets, net	137,159	83,634
Purchased intangible assets, net	748,892	263,767
Goodwill	1,159,651	561,414
Deferred tax assets	213,676	205,496
Other assets	81,965	38,802
Total assets	$3,440,360	$2,313,561
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$183,601	$144,278
Accruals and other current liabilities	252,280	218,123
Deferred revenue, net	101,089	68,824
Senior convertible notes	—	266,981
Short-term debt	53,329	5,074
Total current liabilities	590,299	703,280
Deferred revenue, net	30,070	31,467
Deferred tax liabilities	228,192	92,594
Long-term debt	1,268,510	211,756
Other long-term liabilities	69,586	78,971
Total liabilities	2,186,657	1,118,068
Redeemable noncontrolling interest in subsidiary	893	855
Stockholders' equity:		
VeriFone Systems, Inc. stockholders' equity:		
Preferred Stock: 10,000 shares authorized as of July 31, 2012 and October 31, 2011; no shares issued and outstanding as of July 31, 2012 and October 31, 2011	—	—
Common stock: $0.01 par value, 200,000 shares authorized as of July 31, 2012 and October 31, 2011; 107,920 and 105,826 shares issued and 107,791 and 105,697 outstanding as of July 31, 2012 and October 31, 2011	1,079	1,058
Additional paid-in capital	1,529,311	1,468,862
Accumulated deficit	(231,007)	(269,056)
Accumulated other comprehensive loss	(82,583)	(6,671)

Total stockholders' equity	1,216,800	1,194,193
Noncontrolling interest in subsidiaries	36,010	445
Total liabilities and equity	$3,440,360	$2,313,561

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

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VERIFONE SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended July 31	
	2012	2011
	(Unaudited)	
	(In thousands)	
Cash flows from operating activities		
Consolidated net income	$38,415	$83,799
Adjustments to reconcile consolidated net income to net cash provided by operating activities:		
Depreciation and amortization, net	129,819	24,205
Stock-based compensation expense	34,171	25,107
Non-cash interest expense	12,405	11,560
Deferred income taxes	(15,576)	1,744
Other	102	(4,375)
Net cash provided by operating activities before changes in operating assets and liabilities	199,336	142,040
Changes in operating assets and liabilities, net of effects of business acquisitions:		
Accounts receivable, net	(59,562)	(62,866)
Inventories, net	(4,233)	8,280
Prepaid expenses and other assets	(26,664)	(17,388)
Accounts payable	23,371	31,975
Deferred revenue, net	31,758	5,468
Other current and long term liabilities	(18,643)	14,145
Net change in operating assets and liabilities	(53,973)	(20,386)
Net cash provided by operating activities	145,363	121,654
Cash flows from investing activities		
Capital expenditures	(44,555)	(9,288)
Acquisitions of businesses, net of cash and cash equivalents acquired	(1,069,412)	(10,756)
Collection of other notes receivable	12,595	—
Other investing activities, net	1,111	750
Net cash used in investing activities	(1,100,261)	(19,294)
Cash flows from financing activities		
Proceeds from debt, net of issue costs	1,414,447	73
Repayments of debt	(357,198)	(8,024)
Repayment of senior convertible notes, including interest	(279,159)	—
Proceeds from issuance of common stock through employee equity incentive plans	28,683	41,152
Payments of acquisition related contingent considerations	(23,804)	—
Distribution to non-controlling interest stockholders	(1,543)	(280)
Tax benefit from stock-based compensation	—	556
Net cash provided by financing activities	781,426	33,477
Effect of foreign currency exchange rate changes on cash and cash equivalents	(11,283)	3,226
Net increase (decrease) in cash and cash equivalents	(184,755)	139,063
Cash and cash equivalents, beginning of period	594,562	445,137
Cash and cash equivalents, end of period	$409,807	$584,200

Schedule of non-cash transactions		
Issuance of common stock for business acquisition	$—	$51,090

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

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VERIFONE SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
Note 1. Principles of Consolidation and Summary of Significant Accounting Policies

Basis of Presentation
The accompanying unaudited condensed consolidated financial statements of VeriFone Systems, Inc. (“we,” “us,” “our,” "VeriFone," and “the Company” refer to VeriFone Systems, Inc. and its consolidated subsidiaries) as of July 31, 2012 and October 31, 2011, and for the three and nine months ended July 31, 2012 and 2011, have been prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP") for interim financial information and with the instructions on Form 10-Q pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). In accordance with those rules and regulations, we have omitted certain information and notes normally provided in our annual consolidated financial statements. In the opinion of management, the unaudited condensed consolidated financial statements contain all adjustments, consisting only of normal recurring items necessary for the fair presentation of our financial position and results of operations for the interim periods. These unaudited condensed consolidated financial statements should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended October 31, 2011. The results of operations for the three and nine months ended July 31, 2012 are not necessarily indicative of the results expected for the entire fiscal year. All significant inter-company accounts and transactions have been eliminated. Amounts pertaining to the noncontrolling ownership interests held by third parties in the operating results and financial position of our majority-owned subsidiaries are reported as 'net income attributable to noncontrolling interests' in our Condensed Consolidated Statements of Operations and as 'redeemable noncontrolling interest in subsidiary' on our Condensed Consolidated Balance Sheets when the third party ownership interest is redeemable at the option of the stockholder, outside of our control, and as 'noncontrolling interest in subsidiaries' on our Condensed Consolidated Balance Sheets in all other cases.
The condensed consolidated balance sheet at October 31, 2011 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements.
Certain prior period amounts reported in our Condensed Consolidated Financial Statements and notes thereto have been reclassified to conform to the current period presentation, with no impact on previously reported operating results or financial position.
Use of Estimates

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. The estimates and judgments affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent liabilities.

On an ongoing basis, we evaluate our estimates including those related to product returns, bad debts, inventories, goodwill and intangible assets, income taxes, warranty obligations, contingencies, stock-based compensation and litigation, among others. We base our estimates on historical experience and information available to us at the time that these estimates are made. Actual results could differ materially from these estimates.
Summary of Significant Accounting Policies

There have been no changes to our significant accounting policies during the nine months ended July 31, 2012 as compared with the significant accounting policies described in our audited consolidated financial statements included in our Annual Report on Form 10-K for the fiscal year ended October 31, 2011, except for the two additions below.
Debt Issuance Costs

Debt issuance costs are stated at cost, net of accumulated amortization in Other assets on the Condensed Consolidated Balance Sheets. Amortization expense is calculated using the effective interest method over the period of the loans and is recorded in Interest expense in the accompanying Condensed Consolidated Statements of Operations. At July 31, 2012, interest amortization periods range from 5 to 7 years based upon the maturity date of the related outstanding debt.

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Revenue Generating Assets, Net

Revenue generating assets are comprised of tangible assets that we have placed at third party locations for the purpose of generating revenues, such as in taxi cabs, at gas stations and in small merchant locations, under rental or service based arrangements. Revenue generating assets are stated at cost, net of accumulated depreciation, and are depreciated on a straight-line basis over the estimated useful lives of the assets, generally five years. Payments to acquire revenue generating assets are included in capital expenditures as a cash flow from investing activities on our Condensed Consolidated Statements of Cash Flows.

Concentrations of Credit Risk

No customer accounted for more than 10% of net revenues in any of our reportable segments for the three and nine months ended July 31, 2012 and 2011. As of July 31, 2012, one customer, Redecard S/A, accounted for 10% of total accounts receivable in our International segment. At October 31, 2011, one customer, Cielo S.A. and its affiliates, accounted for 10% of our total accounts receivable in our International segment. No customer accounted for more than 10% of accounts receivable in our North America segment or total accounts receivable as of July 31, 2012 or October 31, 2011.

Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standard Board (“FASB”) issued Accounting Standards Update (“ASU”) 2011-05, Comprehensive Income (Topic 220)—Presentation of Comprehensive Income, which requires an entity to present the total comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of equity. In December 2011, the FASB issued ASU 2011-12, Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. ASU 2011-12 defers the effective date of the requirement in ASU 2011-05 to disclose on the face of the financial statements the effects of the reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income. All other requirements in ASU 2011-05 are not affected by ASU 2011-12. ASU 2011-05 and ASU 2011-12 are effective for us in our first quarter of fiscal year 2013. We have historically presented the components of other comprehensive income as part of our Consolidated Statements of Equity, and therefore adoption of this guidance will change our financial statement presentation.

Note 2. Business Combinations

Point Acquisition

On December 30, 2011, we completed our acquisition of Electronic Transaction Group Nordic Holding AB, a Swedish company operating the Point International business (collectively, "Point"), Northern Europe's largest provider of payment and gateway services and solutions for retailers. The purchase price was approximately €600.0 million, plus repayment of Point's outstanding debt, for a total cash purchase price of $1,024.5 million. The source of funds for the cash consideration was a new credit agreement provided by a syndicate of banks ("the 2011 Credit Agreement"). See Note 5. Financings for information on the 2011 Credit Agreement.

As a result of the acquisition, Point became a wholly-owned subsidiary of VeriFone. The acquisition was accounted for using the acquisition method of accounting. One subsidiary of Point, Babs Paylink AB, is owned 51% by Point and 49% by a third party that has a noncontrolling interest. The results of operations for the acquired businesses have been included in our financial results since the acquisition date.

We acquired Point to, among other things, provide a broader set of product and service offerings to customers globally, including expansion in the Northern European markets. For the three and nine months ended July 31, 2012, we estimate that our total net revenues increased by approximately $55.9 million and $131.3 million, respectively, due to the sale of products and services by Point entities. For the three and nine months ended July 31, 2012, the acquired Point business negatively impacted our earnings by approximately $7.0 million and $29.0 million, respectively, which included management's allocations and estimates of expenses that were not separately identifiable due to our integration activities, non-recurring charges associated with the fair value decrease ("step-down") in deferred revenue, amortization, and acquisition and integration expenses.

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The fair value of consideration transferred for Point was comprised of (in thousands):

Cash paid to Point stockholders	$774,268
Cash for repayment of long-term debt	250,264
Total	$1,024,532

Recording of Assets Acquired and Liabilities Assumed

The assets acquired and liabilities assumed as part of our acquisition of Point were recognized at their fair values as of the acquisition date, December 30, 2011. We recorded the net tangible and intangible assets acquired and liabilities assumed based upon their preliminary fair values as of the acquisition date, as set forth below. The fair values were based upon a preliminary valuation, and our estimates and assumptions are subject to change within the measurement period (up to one year from the acquisition date). The primary areas of the preliminary purchase price allocation that are not yet finalized are the fair values of certain acquired tangible and intangible assets and liabilities, such as inventories and fixed assets, as well as pre-acquisition contingencies including acquisition and divestiture related claims, income and non-income based taxes, and residual goodwill. We expect to continue to obtain information during the measurement period to assist us in determining the fair values assigned to the assets acquired and liabilities assumed at the acquisition date.

The following table summarizes the estimated fair values assigned to the assets acquired and liabilities assumed, as of the acquisition date, which are considered preliminary and thus subject to change (in thousands):

Cash and cash equivalents	$25,314	
Accounts receivable (gross contractual value of $24.5 million, of which $1.7 million is not expected to be collected)	22,691	
Inventories	25,543	
Deferred tax assets	13,020	
Prepaid expenses and other assets	48,304	
Property, plant and equipment	10,350	
Intangible assets	567,007	
Accounts payable and other liabilities	(51,564	)
Contingent consideration payable	(21,233	)
Deferred revenue, net	(2,169	)
Deferred tax liabilities	(157,411	)
Noncontrolling interest in subsidiary	(36,764	)
Total identifiable net assets	443,088	
Goodwill	581,444	
Total consideration transferred	$1,024,532	

During the six months ended July 31, 2012, new information was obtained about the acquisition date fair values of certain of the above assets acquired and liabilities assumed. As a result, we have increased our fair value estimates for acquired intangible assets by $16.5 million, decreased the fair value estimate of non-controlling interests by $0.4 million, and decreased the fair value estimates of other net tangible assets acquired by $3.8 million. Goodwill decreased by $13.1 million due to these changes in fair value estimates.

Goodwill is calculated as the excess of the consideration transferred over the identifiable net assets and represents future benefits arising from other assets acquired that could not be individually identified and separately recognized. Specifically, the goodwill recorded as part of the acquisition of Point includes the expected synergies and other benefits that we believe will result from combining the operations of Point with the operations of VeriFone and the value of the going-concern element of Point's business (which represents the higher rate of return on the assembled collection of net assets versus if VeriFone acquired all of the net assets separately). We generally do not expect the goodwill recognized to be deductible for income tax purposes.

The estimated fair value of acquired contingent consideration owed by Point related to its prior acquisitions was $21.2 million as of the acquisition date. This contingent consideration will be payable in cash if certain operating and financial targets are achieved in the two years following the dates of those acquisitions. The payout criteria for the contingent consideration contains provisions for prorated payouts if the target criteria are not met, provided that certain minimum thresholds are achieved. The U.S. dollar equivalent maximum payout for this contingent consideration as of the acquisition date was $24.4 million.

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The fair value of the noncontrolling interest in Babs Paylink AB of $36.8 million was estimated by employing an income approach based on an assumed discount rate of 17% and an estimated terminal value derived from terminal stabilized cash flow multiples ranging from 8 to 9.

Valuations of Intangible Assets Acquired

The following table sets forth the components of intangible assets acquired in connection with the Point acquisition (in thousands, except for estimated useful lives):

	Fair Value	Estimated Useful Life (Years)
Customer relationships	$498,503	9.5
Developed software technology	54,783	4.4
Trade names	13,721	4.0
Total	$567,007	

Customer relationships represent the fair value of the underlying relationship and agreement with Point customers.

Developed software technology represents the fair values of Point's proprietary technologies, processes, patents and trade secrets related to the design of Point's products that have reached technological feasibility and are a part of Point's product lines.

Trade names represent the fair value of the Point and other trademarks owned by Point.

Some of the more significant estimates and assumptions inherent in the estimates of the fair values of identifiable intangible assets include all assumptions associated with forecasting product profitability from the perspective of a market participant. Specifically:

- Revenue - we use historical, forecast, and industry or other sources of market data, including the number of units to be sold, selling prices, market penetration, market share, and year-over-year growth rates over the product life cycles.

- Cost of sales, research and development expenses, sales and marketing expenses and general administrative expenses - we use historical, forecast, industry, or other sources of market data, including any expected synergies that can be realized by a market participant.

- Estimated life of the asset - we assess the asset's life cycle by considering the impact of technology changes and applicable payment security compliance and regulatory requirements.

- Discount rates - we use a discount rate that is based on the weighted average cost of capital with adjustments to reflect the risks associated with the specific intangible assets, such as country risks and commercial risks.

- Customer attrition rates - we use historical and forecast data to determine the customer attrition rates and the expected customer life.

The discount rates used in the intangible asset valuations ranged from 14% to 20%. The customer attrition rates used in our valuation of customer relationship intangible assets ranged from zero to 7% depending on the geographic region. The estimated life of developed software technology intangible assets ranged from 2 years to 10 years. The royalty rate used in the valuation of the trade names intangible asset ranged from 1% to 2%. All of these judgments and estimates can materially impact the fair values of intangible assets.

Preliminary Pre-Acquisition Contingencies Assumed

We have evaluated and will continue to evaluate pre-acquisition contingencies relating to Point that existed as of the acquisition date. We have preliminarily determined that certain of these pre-acquisition contingencies are probable in nature and estimable as of the acquisition date and, accordingly, have preliminarily recorded our best estimates for these contingencies. If we make changes to the amounts recorded or identify additional pre-acquisition contingencies during the remainder of the measurement period, such amounts recorded will be included in the purchase price allocation during the measurement period and, subsequently, in our results of operations. The largest recorded contingent obligations relate to earn-out obligations associated with Point's prior acquisitions.

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Other Fiscal Year 2012 Acquisitions

During the nine months ended July 31, 2012, in addition to Point, we completed the acquisitions of other businesses and net assets as described in the table below for an aggregate purchase price of $81.5 million. The $81.5 million aggregate purchase price includes $6.4 million of holdback payments that will be paid between 12 to 15 months after the date the respective acquisitions closed, and contingent consideration having a total fair value of $4.4 million. The holdback amounts will be paid out to selling stockholders unless the general representations and warranties made by the sellers as of the acquisition date were invalid. The contingent consideration will be payable in cash for the ChargeSmart (now known as VeriFone Commerce Solutions, Inc.) and LIFT acquisitions, if certain operating and financial targets are achieved in the first three years of operations after the acquisition. The payout criteria for the contingent consideration contain provisions for prorated payouts if the target criteria are not met, provided that certain minimum thresholds are achieved. The contingent consideration was valued at $0.4 million and $4.0 million for the ChargeSmart and LIFT acquisitions, respectively. The maximum payouts for the contingent consideration under the purchase agreements are $11.0 million and $8.0 million for the ChargeSmart and LIFT acquisitions, respectively. The acquisition of each company was accounted for using the acquisition method of accounting. No VeriFone equity interests were issued, and in each transaction 100% of the voting equity interests of the applicable business was acquired except for Show Media, which was structured as an acquisition of assets and assumption of certain liabilities. The results of operations for the acquired businesses have been included in our financial results since their respective acquisition dates.

The below table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date of each transaction. Certain fair values assigned are preliminary and thus subject to change. In particular, the estimated fair values of income and non-income based taxes, LIFT contingent consideration, and residual goodwill are preliminary.

(in thousands)	LIFT	ChargeSmart	Show Media	Global Bay	Total
Acquisition date	March 1, 2012	January 3, 2012	November 1, 2011	November 1, 2011	
Assets acquired (liabilities assumed), net	$(10)	$(4,225)	$1,593	$(5,028)	$(7,670)
Intangible assets (1)	1,600	9,770	6,660	14,490	32,520
Goodwill (2)	4,904	13,829	19,871	18,050	56,654
Total purchase price	$6,494	$19,374	$28,124	$27,512	$81,504

Explanatory notes:

(1) Intangible assets included developed technology, customer relationships, non-compete agreement, trademarks and in-process research and development of $21.3 million, $6.5 million, $3.0 million, $0.9 million and $0.8 million, respectively, which are amortized over their estimated useful lives of 1 to 10 years.

(2) Goodwill is generally not expected to be tax deductible for LIFT, ChargeSmart and Global Bay, but is expected to be deductible for tax purposes for Show Media. The amount of goodwill resulted primarily from our expectation of increased value resulting from the integration of the acquired businesses' product offerings with our product offerings.

Fiscal Year 2011 Acquisitions

Hypercom Corporation

On August 4, 2011, we completed our acquisition of Hypercom, a provider of electronic payment solutions and value-added services at the point of transaction, by means of a merger of one of our wholly-owned subsidiaries with and into Hypercom such that Hypercom became a wholly-owned subsidiary of VeriFone following the merger. We acquired Hypercom to, among other things, provide a broader set of product and service offerings to customers globally. We have included the financial results of Hypercom in our Condensed Consolidated Financial Statements from the date of acquisition.

For the three and nine months ended July 31, 2012, we estimate that our total net revenues increased by approximately $68.5 million and $223.0 million, respectively, due to the sale of Hypercom products and services. Other revenues and earnings contributions from Hypercom were not separately identifiable due to our integration activities.

The total fair value of consideration transferred was $644.6 million which consisted of $557.1 million of VeriFone stock issued, $16.2 million for the fair value of stock options assumed, and $71.2 million for the cash used to repay Hypercom's long-term debt. We recorded the preliminary fair value of assets acquired and liabilities assumed of approximately $363.5 million of goodwill, $210.7 million of intangible assets and $70.4 million of net tangible assets. During the nine months ended July 31, 2012, we adjusted the

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preliminary valuation of the acquired net tangible assets of Hypercom based upon information that was gathered about acquisition date fair values. The adjustments primarily related to finalizing the fair value assessment of sales-type lease receivables, which resulted in a $2.4 million increase in the value of those lease receivables, recording a tax receivable of $2.6 million for tax refunds related to pre-acquisition tax periods, reflecting a $3.3 million increase in the fair value estimate for pre-acquisition liabilities associated with Hypercom's divestitures of its UK and Spain operations, reducing the fair value estimate for certain fixed assets by $2.1 million following completion of the fair value assessment, recording a legal accrual of $2.1 million related to a pre-acquisition claim, increasing the deferred tax asset by $0.5 million related to the fair value adjustments and completion of the pre-acquisition U.S. income tax return, and decreasing the fair value of other liabilities by $0.3 million. As a result of these changes and other immaterial items, goodwill increased by $1.7 million. As of July 31, 2012, we have completed our fair value assessment of Hypercom's acquired assets and assumed liabilities.

Pro Forma Financial Information

The supplemental pro forma financial information below was prepared using the acquisition method of accounting and is based on the historical financial information of VeriFone, Point, Hypercom and other acquired businesses, reflecting results of operations for the three and nine month periods ended July 31, 2012 and 2011 on a comparative basis as though the aforementioned companies were combined as of the beginning of fiscal year 2011. The pro forma financial information includes adjustments to reflect one time charges and amortization of fair value adjustments in the appropriate pro forma periods as though the companies were combined as of the beginning of fiscal year 2011. These adjustments include:

- Net adjustments to amortization expense related to the fair value of acquired identifiable intangible assets totaling $(1.6) million and $4.4 million for the three and nine months ended July 31, 2012, respectively, and $25.7 million and $83.7 million for the three and nine months ended July 31, 2011, respectively.

- Additional interest expense of $4.1 million for the period from November 2011 through December 2011, and $3.7 million and $11.8 million for the three and nine months ended July 31, 2011, respectively, that would be incurred on additional borrowings made to fund the acquisitions, offset by elimination of acquired business interest expense on borrowings that were settled as part of the acquisitions. No adjustment is included for interest after December 2011 as the additional interest is reflected in our operating results following the date the borrowings actually occurred.

- Adjustments for other (charges) benefits, such as closing costs, one time professional fees, foreign currency losses related to deal consideration, amortization of fair market value adjustments and net tax effect of all of these, totaling $(5.6) million and $(55.7) million for the three and nine months ended July 31, 2012, respectively, and $(3.9) million and $25.1 million for the three and nine months ended July 31, 2011, respectively.

The supplemental pro forma financial information for the three and nine months ended July 31, 2012 combines the historical results of VeriFone for the three and nine months ended July 31, 2012, the historical results of Point and ChargeSmart for the two months ended December 31, 2011, the historical results of LIFT for the four months ended February 29, 2012, and the effects of the pro forma adjustments listed above. The results of each acquired company is included as part of VeriFone historical results following the closing date of the particular acquisition.

The supplemental pro forma financial information for the three and nine months ended July 31, 2011 combines the historical results of VeriFone for the three and nine months ended July 31, 2011, the historical results of all fiscal year 2011 and fiscal year 2012 acquired businesses for the three and nine months ended July 31, 2011 based upon their respective previous reporting periods, the dates that these companies were acquired by us, and the effects of the pro forma adjustments listed above.

The following table presents supplemental pro forma financial information as if all acquisitions since the beginning of fiscal year 2011 occurred on November 1, 2010 (unaudited; in thousands except per share data):

	For the Three Months Ended July 31,		For the Nine Months Ended July 31,	
	2012	2011	2012	2011
Total revenues	$492,205	$465,891	$1,431,101	$1,348,337
Net income	$44,865	$(9,594)	$86,437	$(56,249)
Net income per share attributable to VeriFone Systems, Inc. stockholders - basic	$0.42	$(0.09)	$0.81	$(0.54)
Net income per share attributable to VeriFone Systems, Inc. stockholders - diluted	$0.41	$(0.09)	$0.78	$(0.54)

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Acquisition-related Costs

Acquisition-related costs consist of (i) transaction costs, which represent external costs directly related to our acquisitions and primarily include expenditures for professional fees such as banking, legal, accounting and other directly related incremental costs incurred to close the acquisition and (ii) integration costs, which represent personnel related costs for transitional and certain other employees, integration related professional services, additional asset write offs and other integration activity related expenses. The following table presents a summary of acquisition-related costs for the three and nine months ended July 31, 2012 (in thousands):

	For the three months ended July 31, 2012			For the nine months ended July 31, 2012		
	Transaction Costs	Integration Costs	Total	Transaction Costs	Integration Costs	Total
Cost of net revenues	$3	$1,026	$1,029	$12	$5,699	$5,711
Research and development	—	1,060	1,060	—	3,962	3,962
Sales and marketing	12	695	707	195	1,735	1,930
General and administrative	505	2,613	3,118	8,094	15,678	23,772
	$520	$5,394	$5,914	$8,301	$27,074	$35,375

The following table presents a summary of acquisition-related costs for the three and nine months ended July 31, 2011 (in thousands):

	For the three months ended July 31, 2011			For the nine months ended July 31, 2011		
	Transaction Costs	Integration Costs	Total	Transaction Costs	Integration Costs	Total
Cost of net revenues	$23	$27	$50	$151	$226	$377
Research and development	8	33	41	14	51	65
Sales and marketing	476	283	759	669	308	977
General and administrative	2,920	2,422	5,342	8,015	3,626	11,641
	$3,427	$2,765	$6,192	$8,849	$4,211	$13,060

Note 3. Goodwill and Purchased Intangible Assets

Goodwill

Activity related to goodwill consisted of the following (in thousands):

	Nine Months Ended July 31, 2012	Year Ended October 31, 2011
Balance at beginning of period	$561,414	$169,322
Additions related to current period acquisitions	638,117	392,723
Adjustments related to prior fiscal year acquisitions	1,347	622
Currency translation adjustments	(41,227)	(1,253)
Balance at end of period	$1,159,651	$561,414

Based on our review for potential indicators of impairment performed during the nine months ended July 31, 2012 and the fiscal year ended October 31, 2011, there were no indicators of impairment.

As of July 31, 2012, we had accumulated goodwill impairment losses of $372.4 million and $65.5 million in our International and North America segments, respectively, excluding impacts of foreign currency fluctuations. As of October 31, 2011, we had accumulated goodwill impairment losses of $372.4 million and $65.5 million in our International and North America segments, respectively, excluding impacts of foreign currency fluctuations.

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Purchased Intangible Assets

Purchased intangible assets consisted of the following (in thousands, except weighted-average useful life):

	July 31, 2012			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted-Average Useful Life
Customer relationships	$672,632	$(75,556)	$597,076	8.4
Developed and core technology	152,163	(35,576)	116,587	4.0
In-process research and development	18,018	—	18,018	Indefinite
Trade names	17,675	(3,569)	14,106	4.0
Other	4,885	(1,780)	3,105	6.0
	$865,373	$(116,481)	$748,892	

	October 31, 2011			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted-Average Useful Life
Customer relationships	$185,872	$(16,615)	$169,257	5.5
Developed and core technology	187,193	(114,112)	73,081	4.0
In-process research and development	19,021	—	19,021	Indefinite
Trade names	2,692	(897)	1,795	3.3
Other	3,031	(2,418)	613	3.6
	$397,809	$(134,042)	$263,767	

Amortization of purchased intangible assets for the three and nine months ended July 31, 2012 and 2011 was allocated as follows (in thousands):

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2012	2011	2012	2011
Included in cost of net revenues	$10,582	$2,687	$29,782	$10,713
Included in operating expenses	23,177	1,980	60,552	5,959
	$33,759	$4,667	$90,334	$16,672

Total future amortization expense for purchased intangible assets that have finite lives, based on our existing intangible assets and their current estimated useful lives as of July 31, 2012, is estimated as follows (in thousands):

Fiscal Years Ending October 31:	Cost of Net Revenues	Operating Expenses	Total
Remainder of fiscal 2012	$10,037	$22,929	$32,966
2013	38,548	89,413	127,961
2014	37,737	88,802	126,539
2015	17,687	87,548	105,235
2016	10,409	83,032	93,441
Thereafter	1,104	243,628	244,732
	$115,522	$615,352	$730,874

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Note 4. Balance Sheet and Statement of Income Details
Restricted Cash

The 2011 Credit Agreement required that we fund an escrow account to repay, at maturity, the principal and interest of our 1.375% senior convertible notes due June 2012. As a result, at the closing of our 2011 Credit Agreement in December 2011, we deposited $279.2 million in an escrow account. These escrowed funds were used to repay the senior convertible notes in full upon their maturity in June 2012.

Inventories
Inventories consisted of the following (in thousands):

	July 31, 2012	October 31, 2011
Raw materials	$50,927	$45,716
Work-in-process	2,357	859
Finished goods	111,589	97,741
Total inventories	$164,873	$144,316

Prepaid Expenses and Other Current Assets
Prepaid expenses and other current assets consisted of the following (in thousands):

	July 31, 2012	October 31, 2011
Deferred income taxes	$45,018	$39,040
Prepaid taxes	44,891	18,490
Prepaid expenses	41,649	34,115
Other receivables	15,477	27,020
Investments in equity securities and warrants	2,947	6,132
Other current assets	3,185	2,333
Total prepaid expenses and other current assets	$153,167	$127,130

Fixed Assets, Net
Fixed assets, net consisted of the following (in thousands):

	July 31, 2012	October 31, 2011
Revenue generating assets	$88,834	$32,531
Computer hardware and software	61,193	59,056
Machinery and equipment	30,630	27,952
Leasehold improvements	18,956	17,060
Office equipment, furniture and fixtures	6,863	6,278
Buildings	5,997	6,083
Depreciable fixed assets, at cost	212,473	148,960
Accumulated depreciation	(99,278)	(74,696)
Depreciable fixed assets, net	113,195	74,264
Construction in progress	22,939	8,345
Land	1,025	1,025
Fixed assets, net	$137,159	$83,634

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Other Assets

Other assets consisted of the following (in thousands):

	July 31, 2012	October 31, 2011
Debt issuance costs, net	$36,386	$2,749
Long-term restricted cash	12,621	4,804
Capitalized software development costs, net	10,520	6,795
Deposits	8,755	8,662
Other long-term receivables	8,592	8,275
Other long-term assets	5,091	7,517
Total other assets	$81,965	$38,802

Long-term restricted cash consisted mainly of deposits pledged for bank guarantees and irrevocable standby letters of credit.

Accrued Warranty

Activity related to Accrued warranty consisted of the following (in thousands):

	Nine Months Ended July 31, 2012	Year Ended October 31, 2011
Balance at beginning of period	$22,032	$12,747
Warranty charged to cost of net revenues	9,486	17,888
Utilization of warranty accrual	(17,356)	(16,573)
Acquired warranty obligations	348	7,139
Change in estimates	(797)	831
Balance at end of period	13,713	22,032
Less: current portion	(12,842)	(20,358)
Long-term portion	$871	$1,674

Deferred Revenue, net

Deferred revenue, net consisted of the following (in thousands):

	July 31, 2012	October 31, 2011
Deferred revenue	$148,851	$113,154
Deferred cost of revenue	(17,692)	(12,863)
	131,159	100,291
Less: current portion	(101,089)	(68,824)
Long-term portion	$30,070	$31,467

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Accruals and Other Current Liabilities

Accruals and other current liabilities consisted of the following (in thousands):

	July 31, 2012	October 31, 2011
Accrued expenses	$77,735	$74,775
Accrued compensation	49,920	51,515
Accrued liabilities for contingencies	24,115	30,561
Accrued patent litigation loss contingency, including interest (Note 13)	18,619	—
Sales and VAT taxes payable	18,366	6,725
Deferred acquisition consideration payable - current portion	16,299	5,681
Accrued warranty	12,842	20,358
Deferred tax liabilities	9,564	4,960
Income taxes payable	8,866	9,116
Other current liabilities	15,954	14,432
Total accruals and other current liabilities	$252,280	$218,123

Other Long-Term Liabilities

Other long-term liabilities consisted of the following (in thousands):

	July 31, 2012	October 31, 2011
Long-term tax liabilities	$43,762	$51,918
Statutory retirement and pension obligations	9,513	10,292
Deferred acquisition consideration payable - non-current portion	3,043	5,125
Other liabilities	13,268	11,636
Total other long-term liabilities	$69,586	$78,971

Noncontrolling Interest in Subsidiaries

Changes in Noncontrolling interest in subsidiaries are set forth below (in thousands):

	Nine Months Ended July 31, 2012	Year Ended October 31, 2011
Noncontrolling interest in subsidiaries at beginning of period	$445	$572
Additions due to acquisitions	36,793	—
Distributions to non-controlling interest stockholders	(1,543)	(418)
Net income attributable to noncontrolling interest in subsidiaries, net	315	291
Noncontrolling interest in subsidiaries at end of period	$36,010	$445

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Other Income (Expense), net

Other income (expense), net consisted of the following (in thousands):

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2012	2011	2012	2011
Foreign currency exchange gains (losses), net	$1,095	$(488)	$(21,341)	$(3,466)
Gain on convertible notes call option hedge settlement	—	4,554	—	4,554
Gain (loss) on adjustments to acquisition related liabilities	(93)	1,200	(292)	2,591
Gain on bargain purchase of a business, net	—	45	—	1,772
Other income (expense), net	(1,723)	1,002	(1,717)	701
Total other income (expense), net	$(721)	$6,313	$(23,350)	$6,152

We recorded a $22.5 million foreign currency loss in December 2011 related to the difference between the forward rate on contracts purchased to fix the U.S. dollar equivalent of the purchase price for our Point acquisition, and the actual rate on the date of derivative settlement. This loss was partially offset by a $1.5 million gain on the currency we held from the date of the derivative settlement until the funds were transferred to purchase Point.

Note 5. Financings

Borrowings under our financing arrangements as of July 31, 2012 and October 31, 2011 consisted of the following (in thousands):

	July 31, 2012	October 31, 2011
2011 Credit Agreement		
Term A loan	$895,538	$—
Term B loan	230,342	—
Revolving loan	190,000	—
2006 Credit Agreement - Term B loan	—	216,250
Senior convertible notes	—	266,981
Point overdraft facility	4,886	—
Other	1,073	580
Total borrowings	1,321,839	483,811
Less: current portion	(53,329)	(272,055)
Long-term portion	$1,268,510	$211,756

2011 Credit Agreement

On December 28, 2011 (the "Effective Date"), VeriFone, Inc. entered into the 2011 Credit Agreement, which initially consisted of a $918.5 million Term A loan, $231.5 million Term B loan, and $350.0 million Revolving loan, of which $300.0 million was initially funded. As of July 31, 2012, our outstanding borrowings under the 2011 Credit Agreement consisted of a $895.5 million Term A loan, $230.3 million Term B loan and $350.0 million Revolving loan, of which $190.0 million was drawn and outstanding. In August 2012, we drew $100 million under the Revolving loan to repay $100 million of the Term B loan, which carries a higher interest rate.

The key terms of the 2011 Credit Agreement are as follows:

- At VeriFone, Inc.'s option, the Term A loan, Term B loan and Revolving loan bear interest at a “Base Rate” or “Eurodollar Rate” plus an applicable margin, as described below. Base Rate loans bear interest at a per annum rate equal to a margin over the greater of the Federal Funds rate plus 0.50% or the JP Morgan prime rate or the one-, two-, three-or six-month (or, in certain circumstances, nine-, twelve- or less than one month) LIBOR rate plus 1.00%. For the Base Rate Term A loan and Revolving loan, the margin varies between 1.00% to 2.00%

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depending upon our consolidated leverage ratio. For the Base Rate Term B loan, the margin varies between 2.00% to 2.25% depending upon our consolidated leverage ratio with a minimum floor rate of 1.00%. Eurodollar Rate loans bear interest at a margin over the one-, two-, three- or six-month LIBOR rate. For the Eurodollar Term A Loan and Revolving loan, the margin varies between 2.00% to 3.00% depending upon our consolidated leverage ratio. The margin for the Eurodollar Rate Term B loan varies between 3.00% to 3.25% depending upon our consolidated leverage ratio with a minimum LIBOR floor rate of 1.00%.

The terms of the 2011 Credit Agreement require VeriFone, Inc. to comply with financial maintenance covenants. VeriFone, Inc. may not permit its total Leverage Ratio to exceed (i) 4.25 to 1.00, in the case of any fiscal quarter ending on or after November 1, 2011, but prior to November 1, 2012, (ii) 3.75 to 1.00 in the case of any fiscal quarter ending on or after November 1, 2012, but prior to November 1, 2013 and (iii) 3.50 to 1.00, in the case of any fiscal quarter ending on or after November 1, 2013. In addition, VeriFone, Inc. must maintain an interest coverage ratio of at least (i) 3.50 to 1.00, in the case of any fiscal quarter ending prior to November 1, 2012 and (ii) 4.00 to 1.00, in the case of any fiscal quarter ending thereafter. Noncompliance with any of the financial covenants without cure or waiver would constitute an event of default under the 2011 Credit Agreement. The 2011 Credit Agreement also contains customary events of default that include, among others, non-payment of principal, interest or fees, violation of covenants, inaccuracy of representations and warranties, bankruptcy and insolvency events, material judgments, cross defaults to material indebtedness and events constituting a change of control. The occurrence of an event of default could result in the termination of commitments under the 2011 Credit Agreement, the declaration that all outstanding loans are immediately due and payable in whole or in part and the requirement of cash collateral deposits in respect of outstanding letters of credit.

The 2011 Credit Agreement contains certain representations and warranties, certain affirmative covenants, certain negative covenants, certain financial covenants and certain conditions that are customarily required for similar financings. These covenants include, among others:

- A restriction on incurring additional indebtedness, subject to specified permitted debt;
- A restriction on creating certain liens;
- A restriction on mergers and consolidations, subject to specified exceptions;
- A restriction on certain investments, subject to certain exceptions and a suspension if VeriFone, Inc. achieves certain credit ratings; and
- A restriction on entering into certain transactions with affiliates.

Pursuant to a Guaranty, dated as of December 28, 2011 (the "Guaranty"), among certain wholly-owned domestic subsidiaries of VeriFone, Inc. identified therein (the "Guarantors"), obligations under the 2011 Credit Agreement are guaranteed by the Guarantors. Pursuant to a Security Agreement and a Pledge Agreement, each dated as of December 28, 2011 (the "Collateral Agreements") among VeriFone, Inc. and the Guarantors on the one hand and JPMorgan, as collateral agent, on the other hand, obligations under the 2011 Credit Agreement, and the guarantees of such obligations are also secured by a first priority lien and security interest, subject to customary exceptions, in certain assets of VeriFone, Inc. and the Guarantors and equity interests owned by VeriFone, Inc. and the Guarantors in certain of their respective domestic and foreign subsidiaries (limited, in the case of foreign subsidiaries, to 65% of the voting stock of such subsidiaries). Certain equity interests owned by existing and subsequently acquired subsidiaries may also be pledged in the future. Other existing and subsequently acquired or newly-formed domestic subsidiaries of VeriFone, Inc. and the Guarantors, may become Guarantors in the future.

VeriFone, Inc. will pay an undrawn commitment fee ranging from 0.25% to 0.50% per annum (depending on VeriFone, Inc.'s leverage ratio) on the unused portion of the Revolving loan. For letters of credit issued under the Revolving loan, VeriFone, Inc. will pay upon the aggregate face amount of each letter of credit a fronting fee to be agreed to the issuer of the letter of credit together with a fee on all outstanding letters of credit at a per annum rate equal to the margin then in effect with respect to LIBOR-based loans under the Revolving loan.

The outstanding principal balance of the Term A loan is required to be repaid in quarterly installments of the following percentages of the original balance outstanding under the Term A loan: 1.25% for each of the first eight calendar quarters after the Effective Date through the quarter ending December 31, 2013; 2.50% for each of the next eight calendar quarters through the quarter ending December 31, 2015 and 5.00% for each of the calendar quarters ending March 31, 2016, June 30, 2016 and September 30, 2016 with the balance being due at maturity on December 28, 2016. The outstanding principal balance of the Term B loan is required to be repaid in equal quarterly installments of 0.25% with the balance being due at maturity on December 28, 2018. The Revolving loan will terminate on December 28, 2016. Outstanding amounts may also be subject to mandatory prepayment

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with the proceeds of certain asset sales and debt issuances and, in the case of the Term B loan only, from a portion of annual excess cash flows (as determined under the 2011 Credit Agreement) depending on VeriFone, Inc.'s leverage ratio.

On December 28, 2011, VeriFone, Inc. utilized a portion of the proceeds from the 2011 Credit Agreement to repay in full, prior to maturity, all of its previously outstanding loans, together with accrued interest and all other amounts due in connection with such repayment, under the credit agreement entered into on October 31, 2006. The amount of this repayment totaled $216.8 million and following such repayment this credit agreement was terminated. No penalties were due in connection with such repayments.

In addition, the 2011 Credit Agreement required that we fund an escrow account to repay at maturity, or upon earlier conversion at the option of the holders thereof, our 1.375% senior convertible notes due June 15, 2012. As a result, in December 2011, $279.2 million was deposited in the escrow account. This amount was used to repay, in full, the senior convertible notes in June 2012. See "Senior Convertible Notes" below.

We incurred $41.6 million of issuance costs in connection with the 2011 Credit Agreement. These costs were capitalized in Other assets on the Condensed Consolidated Balance Sheets, and the costs are being amortized to interest expense using the effective interest method over the term of the credit facilities, which is 5 or 7 years.

As of July 31, 2012, VeriFone has elected the "Eurodollar Rate" margin option under our borrowings under the 2011 Credit Agreement. As such, the interest rate on the Term A and Revolving loan was 2.75%, which was one month LIBOR plus 2.50% margin, and the interest rate on the Term B loan was 4.25%, which was the higher of one month LIBOR or 1.00% plus 3.25% margin. The unused revolving loan facility's commitment fee was 0.375% and the amount available to draw under the Revolving loan was $160.0 million. In August 2012, we drew $100 million under the Revolving loan to repay $100 million of the Term B loan, which carries a higher interest rate.

As of July 31, 2012, interest margins are 2.50% for the Term A loan and the Revolving loan, and 3.25% for the Term B loan.

We were in compliance with all financial covenants under the 2011 Credit Agreement as of July 31, 2012.

On March 23, 2012, we entered into a number of interest rate swap agreements to effectively convert $500.0 million of the Term Loan A from a floating rate to a 0.71% fixed rate plus applicable margin. The interest rate swaps qualify for hedge accounting treatment as cash flow hedges. The interest rate swaps are effective for the period from March 30, 2012 to March 31, 2015 or 36 months.

Senior Convertible Notes

On June 22, 2007, we issued and sold $316.2 million aggregate principal amount of 1.375% senior convertible notes due June 15, 2012 (the "Notes"). The net proceeds from the offering, after deducting transaction costs, were approximately $307.9 million. We incurred approximately $8.3 million of debt issuance costs. The transaction costs, consisting of the initial purchasers' discounts and offering expenses, were primarily recorded in debt issuance costs, net and were amortized to interest expense using the effective interest method over five years.

The Notes matured on June 15, 2012. Prior to June 15, 2012, we had repurchased and extinguished $38.9 million in aggregate principal amount of our outstanding Notes. Holders of the Notes had the right under certain conditions to convert their Notes prior to maturity at any time on or after March 15, 2012. There were no such conversions of the Notes. Upon maturity of the Notes on June 15, 2012, we repaid the remaining principal amount of $277.3 million, together with accrued and unpaid interest of $4.0 million, in cash.

During the term of the Notes, we paid 1.375% interest per annum on the principal amount of the Notes, semi-annually in arrears on June 15 and December 15 of each year, subject to increase in certain circumstances.

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A summary of interest expense and interest rate on the liability component related to the Notes for the three and nine months ended July 31, 2012 and 2011 is as follows (in thousands, except percentages):

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2012	2011	2012	2011
Interest rate on the liability component	7.6 %	7.6 %	7.6 %	7.6 %
Interest expense related to contractual interest coupon	$466	$953	$2,372	$2,859
Interest expense related to amortization of debt discount	2,087	3,948	10,269	11,502
Total interest expense recognized	$2,553	$4,901	$12,641	$14,361

In connection with the offering of the Notes, we entered into note hedge transactions with affiliates of the initial purchasers (the "Counterparties"), consisting of Lehman Brothers OTC Derivatives ("Lehman Derivatives") and JPMorgan Chase Bank, National Association, London Branch. These note hedge transactions served to reduce the potential dilution upon conversion of the outstanding Notes in the event that the volume weighted average price of our common stock on each trading day of the relevant conversion period or other relevant valuation period for the Notes was greater than $44.02 per share. We terminated the note hedge transaction with Lehman Derivatives in June 2011. The note hedge transactions with the Counterparties other than Lehman Derivatives expired unused on June 15, 2012.

In addition, we sold warrants to the Counterparties whereby they have the option to purchase up to approximately 7.2 million shares of our common stock at a price of $62.356 per share. The warrants expire in equal amounts on each trading day from December 19, 2013 to February 3, 2014.

The cost incurred in connection with the note hedge transactions and the proceeds from the sale of the warrants are included as a net reduction in Additional paid-in capital in the accompanying Condensed Consolidated Balance Sheets as of July 31, 2012 and October 31, 2011.

Point Overdraft Facility

Our 51% majority owned subsidiary of Point, Babs Paylink AB, has an unsecured overdraft facility with Swedbank, the 49% stockholder of Babs Paylink AB, that terminates in December 2012. The overdraft facility limit is Swedish Krona ("SEK") 60.0 million (approximately $8.7 million). The interest rate is the bank's published rate plus a margin of 2.55%. At July 31, 2012, the interest rate was 4.3%. There is a 0.25% commitment fee payable annually in advance, and the overdraft facility is renewable annually on December 31. As of July 31, 2012, SEK 33.6 million (approximately $4.9 million) was outstanding and SEK 26.4 million (approximately $3.8 million) was available.

Other

In July 2011 we entered into an agreement with a bank in Mexico pursuant to which we jointly operate certain automated teller machines (“ATMs”) in Mexico. In connection with this agreement, we agreed to install and maintain these ATMs at third party locations and the bank agreed to provide interest-free cash funding for those ATMs. In connection with this agreement, we were required to provide an irrevocable standby letter of credit in favor of the bank to guarantee our performance under the agreement. During our fiscal quarter ended January 31, 2012, we deposited $2.0 million as collateral for this letter of credit, which is classified as restricted cash on our Condensed Consolidated Balance Sheets as of July 31, 2012. The initial term of the agreement ended on July 14, 2012 and the agreement automatically renewed under its terms for another one-year period. Thereafter, this agreement automatically renews for successive one year periods unless either party gives notice of its intent not to renew as required under the agreement.

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Principal Payments

As of July 31, 2012, principal payments due for financings over the next five years, based on the maturity dates of the debt, are as follows (in thousands):

Fiscal Years Ending October 31:	
2012 (Remainder of the fiscal year)	$12,668
2013	53,176
2014	82,708
2015	94,191
2016	163,070
Thereafter	916,026
	$1,321,839

Note 6. Fair Value Measurements

For assets and liabilities measured at fair value such amounts are based on an expected exit price, representing the amount that would be received on the sale of an asset or paid to transfer a liability, as the case may be, in an orderly transaction between market participants. As such, fair value may be based on assumptions that market participants would use in pricing an asset or liability. The authoritative guidance on fair value measurements, including Accounting Standards Codification 820 Fair Value Measurement and Disclosures and ASU 2011-04, Fair Value Measurement (Topic 820)- Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs establishes a consistent framework for measuring and disclosing fair value on either a recurring or nonrecurring basis whereby inputs, used in valuation techniques, are assigned a hierarchical level. The following are the hierarchical levels of inputs to measure fair value:

Level 1 -	Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.
Level 2 -	Observable inputs that reflect quoted prices for identical assets or liabilities in markets that are not active; quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the assets or liabilities; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.
Level 3 -	Unobservable inputs reflecting our own assumptions incorporated in valuation techniques used to determine fair value. These assumptions are required to be consistent with market participant assumptions that are reasonably available.

Assets and Liabilities Measured and Recorded at Fair Value on a Recurring Basis

There were no transfers between fair value measurement levels during the nine months ended July 31, 2012. The following table presents our assets and liabilities that were measured at fair value on a recurring basis as of July 31, 2012 and October 31, 2011, classified by the level within the fair value hierarchy (in thousands):

	July 31, 2012			
	Carrying Value	Quoted Price in Active Market for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Current assets:				
Cash and cash equivalents				
Money market funds (1)	$77,519	$ 77,519	$—	$—
Prepaid expenses and other current assets				
Marketable equity investment (2)	2,715	2,715	—	—
Equity warrants (3)	232	—	232	—
	11	—	11	—

Foreign exchange forward contracts designated
as cash flow hedges (4)

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Foreign exchange forward contracts not designated as cash flow hedges (4)	304	—	304	—
Other assets				
Israeli severance funds (5)	1,607	$ —	1,607	$—
Total assets measured and recorded at fair value	$82,388	$ 80,234	$ 2,154	$—
Liabilities				
Current liabilities:				
Accruals and other current liabilities				
Acquisition related earn-out payables (6)	$8,325	$ —	$ —	$8,325
Interest rate swaps designated as cash flow hedges (7)	2,511	—	2,511	—
Foreign exchange forward contracts designated as cash flow hedges (4)	77	—	77	—
Foreign exchange forward contracts not designated as cash flow hedges (4)	255	—	255	—
Other long-term liabilities				
Acquisition related earn-out payables (6)	3,044	—	—	3,044
Interest rate swaps designated as cash flow hedges(7)	2,635	—	2,635	—
Total liabilities measured and recorded at fair value	$16,847	$ —	$ 5,478	$11,369

	October 31, 2011			
	Carrying Value	Quoted Price in Active Market for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Current assets:				
Cash and cash equivalents				
Money market funds (1)	$186,530	$ 186,530	$ —	$—
Prepaid expenses and other current assets				
Marketable equity investment (2)	5,450	5,450	—	—
Equity warrants (3)	682	—	682	—
Foreign exchange forward contracts not designated as cash flow hedges (4)	58	—	58	—
Other assets				
Israeli severance funds (5)	2,097	—	2,097	—
Total assets measured and recorded at fair value	$194,817	$ 191,980	$ 2,837	$—
Liabilities				
Current liabilities:				
Accruals and other current liabilities				
Acquisition related earn-out payables (6)	$3,603	$ —	$ —	$3,603
Foreign exchange forward contracts not designated as cash flow hedges (4)	314	—	314	—
Other long-term liabilities				

Acquisition related earn-out payables (6)	3,125	—	—	3,125
Total liabilities measured and recorded at fair value	$7,042	$ —	$ 314	$6,728

Explanatory footnotes:

1.Money market funds are classified as Level 1 because we determine the fair value of the funds using quoted market prices in markets that are active.

2.The marketable equity investment is classified as Level 1 because we determine the fair value using quoted market

prices in markets that are active.
3.The equity warrants are classified as Level 2 because we determine the fair value using the Black-Scholes-Merton valuation model considering quoted market prices for the underlying shares, the treasury risk free interest rate, historic volatility and the remaining contractual term of the warrant.
4.The foreign exchange forward contracts are classified as Level 2 because we determine the fair value using quoted market prices and other observable data for similar instruments in an active market.
5.The Israeli severance funds are classified as Level 2 because there are no quoted market prices, but the fund managers provide a daily redemption value for each of the investments that make up the funds.
6.The acquisition related earn-out payables are classified as Level 3 because we use a probability-weighted expected payout model to determine the expected payout and an appropriate discount rate to calculate the fair value. The key assumptions in applying the approach are the internally forecasted sales and contributions for the acquired businesses, the probability of achieving the sales and contribution targets and an appropriate discount rate. Significant increases in the probability of achieving sales and contribution targets in isolation would result in a significantly higher fair value measurement while significant decreases in the probability of success in isolation would result in a significantly lower fair value measurement. Similarly, significant increases in the discount rate in isolation would result in a significantly lower fair value measurement while significant decreases in the discount rate in isolation would result in a significantly higher fair value measurement. We evaluate changes in each of the assumptions used to calculate fair values of our earn-out payable at the end of each period.
7. Interest rate swaps are classified as Level 2 because we determine the fair value using observable market inputs, such as the one month LIBOR forward pricing curve, as well as credit default spreads reflecting nonperformance risks of VeriFone and that of its counterparties.

Fair Value of Acquisition-Related Earn-out Payables

The following table presents a reconciliation for our earn-out payables measured and recorded at fair value on a recurring basis, using Level 3 significant unobservable inputs (in thousands):

	Nine Months Ended July 31, 2012	Fiscal Year Ended October 31, 2011
Balance at beginning of period	$6,728	$2,960
Additions related to current period business acquisitions	25,651	7,334
Changes in estimates, included in Other income (expense), net	292	(2,443)
Interest expense	400	120
Foreign currency adjustments	213	(743)
Payments	(21,915)	(500)
Balance at end of period	$11,369	$6,728

As of July 31, 2012, the total gross earn-out payable, if all the financial performance targets were met as of July 31, 2012, would have been $29.3 million.

Fair Value of Other Financial Instruments

Other financial instruments consist principally of cash, accounts receivable, accounts payable and long-term debt. The estimated fair value of cash, accounts receivable, and accounts payable approximates their carrying value. The estimated fair value of our Term A loan, Term B loan, and Revolving loan approximates the carrying value because the interest rate on such debt adjusts to market rates on a periodic basis. The Notes, which were carried at cost and were repaid in full at maturity on June 15, 2012, had a fair value of $304.6 million as of October 31, 2011, based on the closing trading price of the Company's stock on October 31, 2011.

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Note 7. Investment in Equity Securities

On February 9, 2010, we invested in Trunkbow International Holdings Ltd. (“Trunkbow”), a Jinan, People’s Republic of China-based mobile payments and value-added service applications company. We paid $5.0 million for 2.5 million shares of common stock and warrants to purchase 500,000 shares of common stock. The warrants have a strike price of $2.00 per share and are exercisable anytime up to 5 years from the closing date. The investment was originally accounted for using the cost method and reflected in Other assets in our Condensed Consolidated Balance Sheets. The allocated costs of the shares and warrants were approximately $4.7 million and $0.3 million, respectively.

On February 3, 2011, Trunkbow's shares began trading on the NASDAQ Global Market. As a result, our investment in Trunkbow shares became marketable, and we reclassified this investment as available-for-sale. Accordingly, our investment in the Trunkbow shares is recorded at fair value which is the quoted market price of the shares. Unrealized gains on the shares and unrealized losses judged to be temporary are included in Accumulated other comprehensive income, a component of Stockholders' equity. Realized gains (losses) on the sale of available-for-sale securities, which will be calculated based on the specific identification method, and declines in value below cost judged to be other-than-temporary, if any, will be recorded in Other income (expense), net in our Condensed Consolidated Statements of Operations, as incurred.

Trunkbow Shares: The fair value of our Trunkbow shares as of July 31, 2012 and October 31, 2011 was estimated at $2.7 million and $5.5 million, respectively. The net unrealized loss included in Accumulated other comprehensive loss as of July 31, 2012 was $1.7 million. We increased the unrealized loss in Accumulated other comprehensive income by $1.9 million and $2.5 million during the three and nine months ended July 31, 2012, respectively.

Trunkbow Warrants: The Trunkbow warrants are derivatives. Accordingly, the warrants are recorded at fair value. We estimated the fair value of the warrants using the Black-Scholes-Merton valuation model. The changes in fair value are recorded as Other income (expense), net, in our Condensed Consolidated Statements of Operations. The fair value of our Trunkbow warrants as of July 31, 2012 and October 31, 2011 was estimated at $0.2 million and $0.7 million, respectively. We reflected a $0.3 million and $0.5 million mark-to-market loss in Other income (expense), net in our Condensed Consolidated Statements of Operations for the three and nine months ended July 31, 2012, respectively.

Note 8. Derivative Financial Instruments

We use derivative financial instruments, primarily forward contracts and swaps, to manage our exposure to foreign currency exchange rate and interest rate risks. Our primary objective in holding derivatives is to reduce the volatility of earnings and cash flows associated with changes in foreign currency exchange rates and interest rates.

Our derivatives expose us to credit risk to the extent that the counterparties may be unable to meet the terms of the agreement. However, we do seek to mitigate such risks by limiting our counterparties to major financial institutions. We do not expect losses as a result of defaults by counterparties. We do not use derivative financial instruments for speculative or trading purposes, nor do we hold or issue leveraged derivative financial instruments.

We recognize the fair value of our outstanding derivative financial instruments at the end of each reporting period as either assets or liabilities on the Condensed Consolidated Balance Sheets. See Note 6. Fair Value Measurements for a presentation of the fair value of our outstanding derivative instruments as of July 31, 2012 and October 31, 2011.

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The following tables present the amounts of gains and losses on our outstanding derivative instruments for the three and nine months ended July 31, 2012 and July 31, 2011 (in thousands):

	Three months ended July 31, 2012			Nine months ended July 31, 2012		
	Net amount of gain (loss) deferred as a component of accumulated other comprehensive loss	Amount of gain (loss) reclassified from accumulated other comprehensive loss into income	Amount of gain (loss) recognized in income immediately	Net amount of gain (loss) deferred as a component of accumulated other comprehensive loss	Amount of gain (loss) reclassified from accumulated other comprehensive loss into income	Amount of gain (loss) recognized in income immediately
Derivatives designated as hedging instruments:						
Interest rate swap agreements (1)	$(2,042)	$ (597)	$—	$(5,145)	$ (798)	$—
Foreign exchange forward contracts (2)	(31)	48	(214)	(31)	48	(214)
	(2,073)	(549)	(214)	(5,176)	(750)	(214)
Derivatives not designated as hedging instruments:						
Foreign exchange forward contracts (3)	—	—	4,940	—	—	(19,451)
Equity warrants (3)	—	—	(303)	—	—	(450)
	—	—	4,637	—	—	(19,901)
	$(2,073)	$ (549)	$4,423	$(5,176)	$ (750)	$(20,115)

	Three months ended July 31, 2011			Nine months ended July 31, 2011		
	Net amount of gain (loss) deferred as a component of accumulated other comprehensive loss	Amount of gain (loss) reclassified from accumulated other comprehensive loss into income	Amount of gain (loss) recognized in income immediately	Net amount of gain (loss) deferred as a component of accumulated other comprehensive loss	Amount of gain (loss) reclassified from accumulated other comprehensive loss into income	Amount of gain (loss) recognized in income immediately
Derivatives designated as hedging instruments:						
Interest rate swap agreements (1)	$—	$ —	$—	$—	$ —	$—
Foreign exchange forward contracts (2)	—	—	—	—	—	—
	—	—	—	—	—	—
Derivatives not designated as hedging instruments:						

Foreign exchange forward contracts (3)	—	—	520	—	—	(2,709)
Equity warrants (3)	—	—				