ITRON INC /WA/
Form 10-Q
August 02, 2011

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

FORM 10-Q

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

For the quarterly period ended June 30, 2011

OR

o 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 000-22418

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

Washington	91-1011792
(State of Incorporation)	(I.R.S. Employer Identification Number)

2111 N Molter Road, Liberty Lake, Washington 99019
(509) 924-9900
(Address and telephone number of registrant's principal executive offices)

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 x 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 x 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	x	Accelerated filer	¨
Non-accelerated filer	o (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 x

As of June 30, 2011 there were outstanding 40,696,130 shares of the registrant's common stock, no par value, which is the only class of common stock of the registrant.

Table of Contents

Itron, Inc.
Table of Contents

Table of Contents

PART I: FINANCIAL INFORMATION
Item 1: Financial Statements (Unaudited)
ITRON, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010 (restated)	2011	2010 (restated)
	(in thousands, except per share data)			
Revenues	$612,401	$567,339	$1,176,092	$1,064,962
Cost of revenues	421,318	393,283	800,899	733,842
Gross profit	191,083	174,056	375,193	331,120
Operating expenses				
Sales and marketing	48,845	40,974	93,493	82,511
Product development	40,931	33,022	81,376	66,062
General and administrative	35,118	33,285	68,449	66,342
Amortization of intangible assets	16,197	16,766	31,794	34,577
Restructuring	1,907	—	1,907	—
Total operating expenses	142,998	124,047	277,019	249,492
Operating income	48,085	50,009	98,174	81,628
Other income (expense)				
Interest income	168	111	476	278
Interest expense	(11,420)	(13,965)	(23,534)	(28,888)
Other income (expense), net	(2,477)	(425)	(4,073)	(1,017)
Total other income (expense)	(13,729)	(14,279)	(27,131)	(29,627)
Income before income taxes	34,356	35,730	71,043	52,001
Income tax (provision) benefit	80	(10,419)	(9,487)	(1,440)
Net income	$34,436	$25,311	$61,556	$50,561
Earnings per common share - Basic	$0.85	$0.63	$1.52	$1.26
Earnings per common share - Diluted	$0.84	$0.61	$1.50	$1.23
Weighted average common shares outstanding - Basic	40,670	40,329	40,608	40,261
Weighted average common shares outstanding - Diluted	41,077	41,161	41,059	41,011

The accompanying notes are an integral part of these condensed consolidated financial statements.

ITRON, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands)

	June 30, 2011 (unaudited)	December 31, 2010
ASSETS		
Current assets		
Cash and cash equivalents	$168,284	$169,477

Accounts receivable, net	377,835	371,662
Inventories	253,079	208,157
Deferred tax assets current, net	55,145	55,351
Other current assets	104,496	77,570
Total current assets	958,839	882,217
Property, plant, and equipment, net	301,458	299,242
Deferred tax assets noncurrent, net	12,714	35,050
Other long-term assets	68,967	28,242
Intangible assets, net	292,930	291,670
Goodwill	1,311,771	1,209,376
Total assets	$2,946,679	$2,745,797
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$268,462	$241,949
Other current liabilities	41,630	49,690
Wages and benefits payable	94,855	110,479
Taxes payable	27,976	19,725
Current portion of debt	234,449	228,721
Current portion of warranty	29,999	24,912
Unearned revenue	49,722	28,258
Total current liabilities	747,093	703,734
Long-term debt	341,121	382,220
Long-term warranty	32,839	26,371
Pension plan benefit liability	69,675	61,450
Deferred tax liabilities noncurrent, net	51,539	54,412
Other long-term obligations	86,942	89,315
Total liabilities	1,329,209	1,317,502
Commitments and contingencies		
Shareholders' equity		
Preferred stock	—	—
Common stock	1,339,504	1,328,249
Accumulated other comprehensive income (loss), net	81,390	(34,974)
Retained earnings	196,576	135,020
Total shareholders' equity	1,617,470	1,428,295
Total liabilities and shareholders' equity	$2,946,679	$2,745,797

The accompanying notes are an integral part of these condensed consolidated financial statements.

ITRON, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	Six Months Ended June 30,	
	2011	2010 (restated)
	(in thousands)	
Operating activities		

Net income	$61,556	$50,561
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	64,299	65,071
Stock-based compensation	9,518	9,121
Amortization of prepaid debt fees	2,265	2,762
Amortization of convertible debt discount	5,336	4,957
Deferred taxes, net	6,081	(8,132)
Other adjustments, net	285	3,306
Changes in operating assets and liabilities, net of acquisition:		
Accounts receivable	(12,106)	(52,124)
Inventories	(36,668)	(40,930)
Other current assets	(21,268)	8,375
Other long-term assets	(22,993)	(763)
Accounts payables, other current liabilities, and taxes payable	16,523	42,463
Wages and benefits payable	(21,531)	19,648
Unearned revenue	24,159	2,365
Warranty	9,510	14,355
Other operating, net	2,726	(3,949)
Net cash provided by operating activities	87,692	117,086
Investing activities		
Acquisitions of property, plant, and equipment	(28,712)	(27,716)
Business acquisition, net of cash equivalents acquired	(14,635)	—
Other investing, net	513	4,495
Net cash used in investing activities	(42,834)	(23,221)
Financing activities		
Payments on debt	(55,630)	(73,881)
Issuance of common stock	2,553	6,812
Other financing, net	(319)	(2,237)
Net cash used in financing activities	(53,396)	(69,306)
Effect of foreign exchange rate changes on cash and cash equivalents	7,345	(9,081)
Increase (decrease) in cash and cash equivalents	(1,193)	15,478
Cash and cash equivalents at beginning of period	169,477	121,893
Cash and cash equivalents at end of period	$168,284	$137,371
Non-cash transactions:		
Property, plant, and equipment purchased but not yet paid, net	$978	$(3,491)
Fair value of contingent and deferred consideration payable for business acquisition	5,108	—
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes, net	$6,842	$9,355
Interest, net of amounts capitalized	15,927	21,178

The accompanying notes are an integral part of these condensed consolidated financial statements.

1

Table of Contents

ITRON, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2011
(UNAUDITED)

In this Quarterly Report on Form 10-Q, the terms “we,” “us,” “our,” “Itron,” and the “Company” refer to Itron, Inc.

Note 1: Summary of Significant Accounting Policies

We were incorporated in the state of Washington in 1977. We provide a portfolio of products and services to utilities for the energy and water markets throughout the world.

Financial Statement Preparation

The condensed consolidated financial statements presented in this Quarterly Report on Form 10-Q are unaudited and reflect entries necessary for the fair presentation of the Consolidated Statements of Operations for the three and six months ended June 30, 2011 and 2010, the Consolidated Balance Sheets as of June 30, 2011 and December 31, 2010, and the Consolidated Statements of Cash Flows for the six months ended June 30, 2011 and 2010 of Itron, Inc. and its subsidiaries. All entries required for the fair presentation of the financial statements are of a normal recurring nature, except as disclosed.

Certain information and notes normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) regarding interim results. These condensed consolidated financial statements should be read in conjunction with the 2010 audited financial statements and notes included in our Annual Report on Form 10-K for the year ended December 31, 2010, as filed with the SEC on February 25, 2011. The results of operations for the three and six months ended June 30, 2011 are not necessarily indicative of the results expected for the full fiscal year or for any other fiscal period.

Basis of Consolidation

We consolidate all entities in which we have a greater than 50% ownership interest or in which we exercise control over the operations. We use the equity method of accounting for entities in which we have a 50% or less investment and exercise significant influence. Entities in which we have less than a 20% investment and where we do not exercise significant influence are accounted for under the cost method. Variable interest entities of which we are the primary beneficiary are consolidated. At June 30, 2011, our investments in variable interest entities and noncontrolling interests were not material. Intercompany transactions and balances have been eliminated upon consolidation.

Business Acquisition

On January 10, 2011, we completed the acquisition of Asais S.A.S. and Asais Conseil S.A.S. (collectively Asais), an energy information management software and consulting services provider, located in France. The acquisition consisted of cash and contingent consideration. The acquisition was immaterial to our financial position, results of operations, and cash flows. (See Business Combinations policy below.)

Cash and Cash Equivalents

We consider all highly liquid instruments with remaining maturities of three months or less at the date of acquisition to be cash equivalents.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are recorded for invoices issued to customers in accordance with our contractual arrangements. Interest and late payment fees are minimal. Unbilled receivables are recorded when revenues are recognized upon product shipment or service delivery and invoicing occurs at a later date. We record an allowance for doubtful accounts representing our estimate of the probable losses in accounts receivable at the date of the balance sheet based on our historical experience of bad debts and our specific review of outstanding receivables. Accounts receivable are written-off against the allowance when we believe an account, or a portion thereof, is no longer collectible.

Inventories

Inventories are stated at the lower of cost or market using the first-in, first-out method. Cost includes raw materials and labor, plus applied direct and indirect costs.

Derivative Instruments

All derivative instruments, whether designated in hedging relationships or not, are recorded on the Consolidated Balance Sheets at fair value as either assets or liabilities. The components and fair values of our derivative instruments, which are primarily interest rate swaps, are determined using the fair value measurements of significant other observable inputs (Level 2), as defined by GAAP. The net fair value of our derivative instruments may switch between a net asset and a net liability depending on market circumstances at the end of the period. We include the effect of our counterparty credit risk based on current published credit default swap rates when the net fair value of our derivative instruments are in a net asset position and the effect of our own nonperformance risk when the net fair value of our derivative instruments are in a net liability position.

For any derivative designated as a fair value hedge, the changes in the fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in earnings. For any derivative designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded as a component of other comprehensive income (OCI) and are recognized in earnings when the hedged item affects earnings. For our hedge of a net investment, the effective portion of any unrealized gain or loss from the foreign currency revaluation of the hedging instrument is reported in OCI as a net unrealized gain or loss on derivative instruments. Ineffective portions of fair value changes or the changes in fair value of derivative instruments that do not qualify for hedging activities are recognized in other income (expense) in the Consolidated Statements of Operations. We classify cash flows from our derivative programs as cash flows from operating activities in the Consolidated Statements of Cash Flows.

Derivatives are not used for trading or speculative purposes. Our derivatives are with major international financial institutions, with whom we have master netting agreements; however, our derivative positions are not disclosed on a net basis. There are no credit-risk-related contingent features within our derivative instruments. Refer to Note 7 and Note 12 for further disclosures of our derivative instruments and their impact on OCI.

Property, Plant, and Equipment

Property, plant, and equipment are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally thirty years for buildings and improvements and three to 10 years for machinery and equipment, computers and purchased software, and furniture. Leasehold improvements are capitalized and amortized over the term of the applicable lease, including renewable periods if reasonably assured, or over the useful lives, whichever is shorter. Construction in process represents capital expenditures incurred for assets not yet placed in service. Costs related to internally developed software and software purchased for internal uses are capitalized and are amortized over the estimated useful lives of the assets. Repair and maintenance costs are expensed as incurred. We have no major planned maintenance activities.

We review long-lived assets for impairment whenever events or circumstances indicate the carrying amount of an asset or asset group may not be recoverable. We have had no significant impairments of long-lived assets. Assets held for sale are classified within other current assets in the Consolidated Balance Sheets, are reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. We had no assets held for sale at June 30, 2011 and December 31, 2010. Gains and losses from asset disposals and impairment losses are classified within the statement of operations according to the use of the asset.

Prepaid Debt Fees

Prepaid debt fees represent the capitalized direct costs incurred related to the issuance of debt and are recorded as noncurrent assets. These costs are amortized to interest expense over the lives of the respective borrowings, including contingent maturity or call features, using the effective interest method, or straight-line method when associated with a revolving credit facility. When debt is repaid early, the related portion of unamortized prepaid debt fees is written-off and included in interest expense.

Business Combinations
On the date of acquisition, the assets acquired, liabilities assumed, and any noncontrolling interests in the acquiree are recorded at their fair values. The acquiree results of operations are also included as of the date of acquisition in our consolidated results. Intangible assets that arise from contractual/legal rights, or are capable of being separated, as well as in-process research and development, are measured and recorded at fair value, and amortized over the estimated useful life. If practicable, assets acquired and liabilities assumed arising from contingencies are measured and recorded at fair value. If not practicable, such assets and liabilities are measured and recorded when it is probable that a gain or loss has occurred and the amount can be reasonably estimated. The residual balance of the purchase price, after fair value allocations to all identified assets and liabilities, represents goodwill. Acquisition-related costs are expensed as incurred. Restructuring costs are generally expensed in periods subsequent to the acquisition date, and changes in deferred tax asset valuation allowances and acquired income tax uncertainties, including penalties and interest, after the measurement period are recognized as a component of the provision for income taxes.

Goodwill and Intangible Assets
Goodwill and intangible assets have resulted from our acquisitions. We use estimates in determining and assigning the fair value of goodwill and intangible assets at acquisition, including estimates of useful lives of intangible assets, the amount and timing of related future cash flows, and fair values of the related operations. Our intangible assets have finite lives, are amortized over their estimated useful lives based on estimated discounted cash flows, and are tested for impairment when events or changes in circumstances indicate the carrying value may not be recoverable.

Goodwill is assigned to our reporting units based on the expected benefit from the synergies arising from each business combination, determined by using certain financial metrics, including the forecasted discounted cash flows associated with each reporting unit. Goodwill is tested for impairment as of October 1 of each year, or more frequently if a significant impairment indicator occurs. Determining the fair value of a reporting unit is judgmental in nature and involves the use of significant estimates and assumptions. We forecast discounted future cash flows at the reporting unit level using risk-adjusted discount rates and estimated future revenues and operating costs, which take into consideration factors such as existing backlog, expected future orders, supplier contracts, and expectations of competitive and economic environments. We also identify similar publicly traded companies and develop a correlation, referred to as a multiple, to apply to the operating results of our reporting units.

Contingencies
A loss contingency is recorded if it is probable that an asset has been impaired or a liability has been incurred and the amount of the loss can be reasonably estimated. We evaluate, among other factors, the degree of probability of an unfavorable outcome and our ability to make a reasonable estimate of the amount of the ultimate loss. Loss contingencies that we determine to be reasonably possible, but not probable, are disclosed. Changes in these factors and related estimates could materially affect our financial position and results of operations.

Bonus and Profit Sharing
We have various employee bonus and profit sharing plans, which provide award amounts for the achievement of annual financial and nonfinancial targets. If management determines it is probable that the targets will be achieved, and the amounts can be reasonably estimated, a compensation accrual is recorded based on the proportional achievement of the financial and nonfinancial targets. Although we monitor and accrue expenses quarterly based on our progress toward the achievement of the annual targets, the actual results at the end of the year may require awards that are significantly greater or less than the estimates made in earlier quarters.

Warranty
We offer standard warranties on our hardware products and large application software products. We accrue the estimated cost of warranty claims based on historical and projected product performance trends and costs. Testing of new products in the development stage helps identify and correct potential warranty issues prior to manufacturing. Continuing quality control efforts during manufacturing reduce our exposure to warranty claims. If our quality control

efforts fail to detect a fault in one of our products, we could experience an increase in warranty claims. We track warranty claims to identify potential warranty trends. If an unusual trend is noted, an additional warranty accrual may be assessed and recorded when a failure event is probable and the cost can be reasonably estimated. Management continually evaluates the sufficiency of the warranty provisions and makes adjustments when necessary. The warranty allowances may fluctuate due to changes in estimates for material, labor, and other costs we may incur to repair or replace projected product failures, and we may incur additional warranty and related expenses in the future with respect to new or established products, which could adversely affect our financial position and results of operations. The long-term warranty balance includes estimated warranty claims beyond one year. Warranty expense is classified within cost of revenues.

Defined Benefit Pension Plans
We sponsor both funded and unfunded defined benefit pension plans for our international employees. We recognize a liability for the projected benefit obligation in excess of plan assets or an asset for plan assets in excess of the projected benefit obligation. We also recognize the funded status of our defined benefit pension plans on our Consolidated Balance Sheets and recognize as a component of OCI, net of tax, the actuarial gains or losses and prior service costs or credits, if any, that arise during the period but that are not recognized as components of net periodic benefit cost.

Revenue Recognition
Revenues consist primarily of hardware sales, software license fees, software implementation, project management services, installation, consulting, and post-sale maintenance support. Revenues are recognized when (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the sales price is fixed or determinable, and (4) collectability is reasonably assured.

The majority of our revenue arrangements involve multiple deliverables, which combine two or more of the following: hardware, meter reading system software, installation, and/or project management services. Revenue arrangements with multiple deliverables are divided into separate units of accounting if the delivered item(s) has value to the customer on a standalone basis and delivery/performance of the undelivered item(s) is probable. The total arrangement consideration is allocated among the separate units of accounting based on their relative fair values and the applicable revenue recognition criteria considered for each unit of accounting. The amount allocable to a delivered item is limited to the amount that we are entitled to collect and that is not contingent upon the delivery/performance of additional items. Revenues for each deliverable are then recognized based on the type of deliverable, such as 1) when the products are shipped, 2) services are delivered, 3) percentage-of-completion when implementation services are essential to other deliverables in the arrangements, 4) upon receipt of customer acceptance, or 5) transfer of title. The majority of our revenue is recognized when products are shipped to or received by a customer or when services are provided.

We primarily enter into two types of multiple deliverable arrangements, which include a combination of hardware and associated software and services:

- Arrangements that do not include the deployment of our smart metering systems and technology are recognized as follows:

  Hardware revenues are recognized at the time of shipment, receipt by customer, or, if applicable, upon completion of customer acceptance provisions.
  If implementation services are essential to the functionality of the associated software, software and implementation revenues are recognized using either the percentage-of-completion methodology of contract accounting if project costs can be estimated, or the completed contract methodology if project costs cannot be reliably estimated.

- Arrangements to deploy our smart metering systems and technology are recognized as follows:

Hardware revenues are recognized at the time of shipment, receipt by customer, or, if applicable, upon completion of customer acceptance provisions.
Revenue from associated software and services is recognized using the units-of-delivery method of contract accounting, as the software is essential to the functionality of the related hardware and the implementation services are essential to the functionality of the associated software. This methodology often results in the deferral of costs and revenues as professional services and software implementation typically commence prior to deployment of hardware.

We also enter into multiple deliverable software arrangements that do not include hardware. For this type of arrangement, revenue recognition is dependent upon the availability of vendor specific objective evidence (VSOE) of fair value for each of the deliverables. The lack of VSOE, or the existence of extended payment terms or other inherent risks, may affect the timing of revenue recognition for software arrangements.

Certain of our revenue arrangements include an extended or noncustomary warranty provision which covers all or a portion of a customer’s replacement or repair costs beyond the standard or customary warranty period. Whether or not the extended warranty is separately priced in the arrangement, a portion of the arrangement’s total consideration is allocated to this extended warranty deliverable. This revenue is deferred and recognized over the extended warranty coverage period. Extended or noncustomary warranties do not represent a significant portion of our revenue.

We allocate consideration to each deliverable in an arrangement based on its relative selling price. We determine selling price using VSOE, if it exists, otherwise we use third-party evidence (TPE). If neither VSOE nor TPE of selling price exists for a unit of accounting, we use estimated selling price (ESP).

VSOE is generally limited to the price charged when the same or similar product is sold separately or, if applicable, the stated renewal rate in the agreement. If a product or service is seldom sold separately, it is unlikely that we can determine VSOE for the product or service. We define VSOE as a median price of recent standalone transactions that are priced within a narrow range. TPE is determined based on the prices charged by our competitors for a similar deliverable when sold separately.

If we are unable to establish selling price using VSOE or TPE, we use ESP in the allocation of arrangement consideration. The objective of ESP is to determine the price at which we would transact if the product or service were regularly sold by us on a standalone basis. Our determination of ESP involves a weighting of several factors based on the specific facts and circumstances of the arrangement. Specifically, we consider the cost to produce the deliverable, the anticipated margin on that deliverable, the selling price and profit margin for similar parts, our ongoing pricing strategy and policies (as evident in the price list established and updated by management on a regular basis), the value of any enhancements that have been built into the deliverable, and the characteristics of the varying markets in which the deliverable is sold. We analyze the selling prices used in our allocation of arrangement consideration on an annual basis. Selling prices are analyzed on a more frequent basis if we experience significant variances in our selling prices or if a significant change in our business necessitates a more timely analysis.

Unearned revenue is recorded when a customer pays for products or services, but the criteria for revenue recognition have not been met as of the balance sheet date. Unearned revenues of $68.7 million and $42.8 million at June 30, 2011 and December 31, 2010 related primarily to professional services and software associated with our smart metering contracts, extended or noncustomary warranty, and prepaid post-contract support. Deferred cost is recorded for products or services for which ownership (typically defined as title and risk of loss) has transferred to the customer, but the criteria for revenue recognition have not been met as of the balance sheet date. Deferred costs were $16.6 million and $10.0 million at June 30, 2011 and December 31, 2010 and are recorded within other assets in the Consolidated Balance Sheets.

Hardware and software post-sale maintenance support fees are recognized ratably over the life of the related service contract. Shipping and handling costs and incidental expenses billed to customers are recorded as revenue, with the associated cost charged to cost of revenues. We record sales, use, and value added taxes billed to our customers on a net basis.

Product and Software Development Costs
Product and software development costs primarily include employee compensation and third party contracting fees. For software we develop to be marketed or sold, we capitalize development costs after technological feasibility is established. Due to the relatively short period of time between technological feasibility and the completion of product and software development, and the immaterial nature of these costs, we generally do not capitalize product and software development expenses.

Stock-Based Compensation
We measure and recognize compensation expense for all stock-based awards made to employees and directors, including stock options, stock sold pursuant to our Employee Stock Purchase Plan (ESPP), and the issuance of restricted stock units and unrestricted stock awards, based on estimated fair values. The fair value of stock options is estimated at the date of grant using the Black-Scholes option-pricing model, which includes assumptions for the dividend yield, expected volatility, risk-free interest rate, and expected life. For ESPP awards, the fair value is the difference between the market close price of our common stock on the date of purchase and the discounted purchase price. For restricted stock units and unrestricted stock awards, the fair value is the market close price of our common stock on the date of grant. We expense stock-based compensation at the date of grant for unrestricted stock awards. For awards with only a service condition, we expense stock-based compensation, adjusted for estimated forfeitures, using the straight-line method over the requisite service period for the entire award. For awards with both performance and service conditions, we expense the stock-based compensation, adjusted for estimated forfeitures, on a straight-line basis over the requisite service period for each separately vesting portion of the award. Excess tax benefits are credited to common stock when the deduction reduces cash taxes payable. When we have tax deductions in excess of the compensation cost, they are classified as financing cash inflows in the Consolidated Statements of Cash Flows.

Loss on Extinguishment of Debt, Net
Upon partial or full redemption of our borrowings, we recognize a gain or loss for the difference between the cash paid and the net carrying amount of the debt redeemed. Included in the net carrying amount is any unamortized premium or discount from the original issuance of the debt. Due to the particular characteristics of our convertible notes, we recognize a gain or loss upon conversion or derecognition for the difference between the net carrying amount of the liability component (including any unamortized discount and debt issuance costs) and the fair value of the consideration transferred to the holder that is allocated to the liability component, which is equal to the fair value of the liability component immediately prior to extinguishment. In the case of an induced conversion, a loss is recognized for the amount of the fair value of the securities or other consideration transferred to the holder in excess of fair value of the consideration issuable in accordance with the original conversion terms of the debt.

Income Taxes
We compute our interim income tax provision through the use of an estimated annual effective tax rate (ETR) applied to year-to-date operating results and specific events that are discretely recognized as they occur. In determining the estimated annual ETR, we analyze various factors, including projections of our annual earnings, taxing jurisdictions in which the earnings will be generated, the impact of state and local income taxes, our ability to use tax credits and net operating loss carryforwards, and available tax planning alternatives. Discrete items, including the effect of changes in tax laws, tax rates, and certain circumstances with respect to valuation allowances or other unusual or non-recurring tax adjustments, are reflected in the period in which they occur as an addition to, or reduction from, the income tax provision, rather than included in the estimated annual ETR.

Deferred tax assets and liabilities are recognized based upon anticipated future tax consequences, in each of the jurisdictions in which we operate, attributable to: (1) the differences between the financial statement carrying amounts of existing assets and liabilities and their respective income tax bases; and (2) operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The calculation of our tax liabilities involves applying complex tax regulations in different tax jurisdictions to our tax positions. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date. A valuation allowance is recorded to reduce the carrying amounts of deferred tax assets if it is not more likely than not that such assets will be realized. We do not record tax liabilities on undistributed earnings of international subsidiaries that are permanently reinvested.

A tax position is first evaluated for recognition based on its technical merits. Tax positions that have a greater than fifty percent likelihood of being realized upon ultimate settlement are then measured to determine amounts to be recognized in the financial statements. This measurement incorporates information about potential settlements with taxing authorities. A previously recognized tax position is derecognized in the first period in which the position no longer meets the more-likely-than-not recognition threshold. We classify interest expense and penalties related to uncertain tax positions and interest income on tax overpayments as part of income tax expense.

Foreign Exchange

Our consolidated financial statements are reported in U.S. dollars. Assets and liabilities of international subsidiaries with a non-U.S. dollar functional currency are translated to U.S. dollars at the exchange rates in effect on the balance sheet date, or the last business day of the period, if applicable. Revenues and expenses for these subsidiaries are translated to U.S. dollars using a weighted average rate for the relevant reporting period. Translation adjustments resulting from this process are included, net of tax, in OCI. Gains and losses that arise from exchange rate fluctuations for monetary asset and liability balances that are not denominated in an entity’s functional currency are included within other income (expense), net in the Consolidated Statements of Operations. Currency gains and losses of intercompany balances deemed to be long-term in nature or designated as a hedge of the net investment in international subsidiaries are included, net of tax, in OCI.

Fair Value Measurements

For assets and liabilities measured at fair value, the GAAP fair value hierarchy prioritizes the inputs used in different valuation methodologies, assigning the highest priority to unadjusted quoted prices for identical assets and liabilities in actively traded markets (Level 1) and the lowest priority to unobservable inputs (Level 3). Level 2 inputs consist of quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in non-active markets; and model-derived valuations in which significant inputs are corroborated by observable market data either directly or indirectly through correlation or other means (inputs may include yield curves, volatility, credit risks, and default rates). We hold no assets or liabilities measured using Level 1 fair value inputs.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. These estimates and assumptions 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 period. Due to various factors affecting future costs and operations, actual results could differ materially from these estimates.

Restatement

The unaudited quarterly financial information for the first three quarters of 2010 was restated in the fourth quarter of 2010. The restatement was made primarily to defer revenue previously recognized on one contract due to a misinterpretation of an extended warranty provision. While the restatement was not deemed material to the first three quarters of 2010, we concluded that the aggregate correction of such amounts would be material to the fourth quarter of 2010. Accordingly, although not material to our financial statements for the first and second quarters of 2010, the results of operations for the three and six months ended June 30, 2010 and cash flows for the six months ended June 30, 2010 have been restated, as well as certain balance sheet components as of June 30, 2010. The consolidated statement of operations, consolidated balance sheet, and consolidated statement of cash flows have been restated, as follows:

Consolidated statement of operations	Three Months Ended June 30, 2010		Six Months Ended June 30, 2010	
	As previously reported	As restated	As previously reported	As restated
	(in thousands, except per share data)			
Revenues	$569,460	$567,339	$1,068,740	$1,064,962
Cost of revenues	393,136	393,283	733,521	733,842
Gross profit	176,324	174,056	335,219	331,120
Operating income	52,277	50,009	85,727	81,628
Income before income taxes	37,998	35,730	56,100	52,001
Income tax (provision) benefit	(11,098)	(10,419)	(2,413)	(1,440)
Net income	26,900	25,311	53,687	50,561
Earnings per common share - Basic	$0.67	$0.63	$1.33	$1.26
Earnings per common share - Diluted	$0.65	$0.61	$1.31	$1.23

Consolidated balance sheet	June 30, 2010	
	As previously reported	As restated
	(in thousands)	
Accounts receivable, net	366,476	366,240
Deferred tax assets noncurrent, net	67,684	68,657
Long-term warranty	22,953	23,274
Other long-term obligations	67,908	71,478
Accumulated other comprehensive loss, net	(116,019)	(116,047)
Retained earnings	83,937	80,811

Consolidated statement of cash flow	Six Months Ended June 30, 2010	
	As previously reported	As restated
	(in thousands)	
Operating activities		
Net income	$53,687	$50,561
Adjustments to reconcile net income to net cash provided by operating activities:		
Deferred taxes, net	(7,159)	(8,132)
Changes in operating assets and liabilities, net of acquisition:		
Accounts receivable	(52,332)	(52,124)
Unearned revenue	(1,205)	2,365
Warranty	14,034	14,355

3

Table of Contents

Note 2: Earnings Per Share and Capital Structure

The following table sets forth the computation of basic and diluted earnings per share (EPS):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in thousands, except per share data)			
Net income available to common shareholders	$34,436	$25,311	$61,556	$50,561
Weighted average common shares outstanding - Basic	40,670	40,329	40,608	40,261
Dilutive effect of convertible notes	—	283	—	206
Dilutive effect of stock-based awards	407	549	451	544
Weighted average common shares outstanding - Diluted	41,077	41,161	41,059	41,011
Earnings per common share - Basic	$0.85	$0.63	$1.52	$1.26
Earnings per common share - Diluted	$0.84	$0.61	$1.50	$1.23

Convertible Notes

We are required, pursuant to the indenture for the convertible notes, to settle the principal amount of the convertible notes in cash and may elect to settle the remaining conversion obligation (stock price in excess of conversion price) in cash, shares, or a combination. We include in the EPS calculation the amount of shares it would take to satisfy the conversion obligation, assuming that all of the convertible notes are converted. The average quarterly closing prices of our common stock were used as the basis for determining the dilutive effect on EPS. The average price of our common stock for the three and six months ended June 30, 2011 did not exceed the conversion price of $65.16 and, therefore, did not have an effect on diluted EPS. The average price of our common stock for the three and six months ended June 30, 2010 exceeded the conversion price of $65.16 and, therefore, approximately 283,000 and 206,000 shares have been included in the diluted EPS calculation for those respective periods.

Stock-based Awards

For stock-based awards, the dilutive effect is calculated using the treasury stock method. Under this method, the dilutive effect is computed as if the awards were exercised at the beginning of the period (or at time of issuance, if later) and assumes the related proceeds were used to repurchase common stock at the average market price during the period. Related proceeds include the amount the employee must pay upon exercise, future compensation cost associated with the stock award, and the amount of excess tax benefits, if any. Approximately 672,000 and 664,000 stock-based awards were excluded from the calculation of diluted EPS for the three and six months ended June 30, 2011, and approximately 308,000 and 385,000 stock-based awards were excluded from the calculation of diluted EPS for the three and six months ended June 30, 2010, respectively, because they were anti-dilutive. These stock-based awards could be dilutive in future periods.

Preferred Stock

We have authorized the issuance of 10 million shares of preferred stock with no par value. In the event of a liquidation, dissolution, or winding up of the affairs of the corporation, whether voluntary or involuntary, the holders of any outstanding preferred stock will be entitled to be paid a preferential amount per share to be determined by the Board of Directors prior to any payment to holders of common stock. Shares of preferred stock may be converted into common stock based on terms, conditions, and rates as defined in the Rights Agreement, which may be adjusted by the Board of Directors. There was no preferred stock sold or outstanding at June 30, 2011 and December 31, 2010.

Table of Contents

Note 3: Certain Balance Sheet Components

Accounts receivable, net	June 30, 2011	December 31, 2010
	(in thousands)	
Trade receivables (net of allowance of $8,980 and $9,045)	$348,736	$328,811
Unbilled receivables	29,099	42,851
Total accounts receivable, net	$377,835	$371,662

At June 30, 2011 and December 31, 2010, $134,000 and $12.5 million were recorded within trade receivables as billed but not yet paid by customers in accordance with contract retainage provisions. At June 30, 2011 and December 31, 2010, contract retainage amounts that were unbilled and classified as unbilled receivables were $4.5 million and $2.1 million. These contract retainage amounts within trade receivables and unbilled receivables are expected to be collected within the following 12 months.

At June 30, 2011 and December 31, 2010, long-term unbilled receivables and long-term retainage contract receivables were $36.5 million and $5.9 million. The increase in long-term receivables from December 31, 2010 to June 30, 2011 includes $12.5 million of retainage contract receivables and $12.0 million of unbilled receivables, which were reclassified to long-term at June 30, 2011 due to a delay in reaching certain contract milestones required for payment. These long-term unbilled receivables and retainage contract receivables are classified within other long-term assets as collection is not anticipated within the following 12 months. However, collection is expected within the following 18 months.

Allowance for doubtful account activity	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in thousands)			
Beginning balance	$9,030	$5,870	$9,045	$6,339
Provision (release) of doubtful accounts, net	298	742	(48)	662
Accounts written-off	(505)	(43)	(552)	(173)
Effects of change in exchange rates	157	(271)	535	(530)
Ending balance	$8,980	$6,298	$8,980	$6,298

Inventories	June 30, 2011	December 31, 2010
	(in thousands)	
Materials	$132,303	$106,021
Work in process	26,058	18,389
Finished goods	94,718	83,747
Total inventories	$253,079	$208,157

Our inventory levels may vary period to period as a result of our factory scheduling and the timing of contract fulfillments, which may include the buildup of finished goods for shipment.

Consigned inventory is held at third-party locations; however, we retain title to the inventory until purchased by the third-party. Consigned inventory, consisting of raw materials and finished goods, was $15.1 million and $17.6 million at June 30, 2011 and December 31, 2010, respectively.

Table of Contents

Property, plant, and equipment, net	June 30, 2011	December 31, 2010
	(in thousands)	
Machinery and equipment	$284,431	$265,113
Computers and purchased software	69,894	63,077
Buildings, furniture, and improvements	150,987	146,661
Land	33,879	35,968
Construction in progress, including purchased equipment	24,600	20,531
Total cost	563,791	531,350
Accumulated depreciation	(262,333)	(232,108)
Property, plant, and equipment, net	$301,458	$299,242

Depreciation expense	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in thousands)			
Depreciation expense	$16,571	$14,994	$32,505	$30,494

Note 4: Intangible Assets

The gross carrying amount and accumulated amortization of our intangible assets, other than goodwill, are as follows:

	June 30, 2011			December 31, 2010		
	Gross Assets	Accumulated Amortization	Net	Gross Assets	Accumulated Amortization	Net
	(in thousands)					
Core-developed technology	$406,570	$(302,669)	$103,901	$378,705	$(274,198)	$104,507
Customer contracts and relationships	307,223	(131,606)	175,617	282,997	(110,539)	172,458
Trademarks and trade names	77,078	(64,196)	12,882	73,194	(59,235)	13,959
Other	11,177	(10,647)	530	24,256	(23,510)	746
Total intangible assets	$802,048	$(509,118)	$292,930	$759,152	$(467,482)	$291,670

A summary of the intangible asset account activity is as follows:

	Six Months Ended June 30,	
	2011	2010
	(in thousands)	
Beginning balance, intangible assets, gross	$759,152	$806,256
Intangible assets acquired	10,297	—
Assets no longer in use written-off	(8,369)	—
Effect of change in exchange rates	40,968	(78,155)
Ending balance, intangible assets, gross	$802,048	$728,101

Intangible assets that were written-off had been fully amortized and were no longer in use. Intangible assets of our international subsidiaries are recorded in their respective functional currency; therefore, the carrying amounts of intangible assets increase or decrease, with a corresponding change in accumulated OCI, due to changes in foreign currency exchange rates.

Table of Contents

Estimated future annual amortization expense is as follows:

Years ending December 31,	Estimated Annual Amortization (in thousands)
2011 (amount remaining at June 30, 2011)	$32,306
2012	50,234
2013	41,442
2014	34,082
2015	27,997
Beyond 2015	106,869
Total intangible assets, net	$292,930

Note 5: Goodwill

The following table reflects goodwill allocated to each reporting segment at June 30, 2011 and 2010:

	Itron North America (in thousands)	Itron International	Total Company
Goodwill balance at January 1, 2010	$197,515	$1,108,084	$1,305,599
Effect of change in exchange rates	89	(159,606)	(159,517)
Goodwill balance at June 30, 2010	$197,604	$948,478	$1,146,082
Goodwill balance at January 1, 2011	$198,048	$1,011,328	$1,209,376
Goodwill acquired	—	10,251	10,251
Effect of change in exchange rates	205	91,939	92,144
Goodwill balance at June 30, 2011	$198,253	$1,113,518	$1,311,771

Note 6: Debt

The components of our borrowings are as follows:

	June 30, 2011 (in thousands)	December 31, 2010
Term loans		
USD denominated term loan	$200,616	$218,642
EUR denominated term loan	151,350	174,031
Convertible senior subordinated notes	223,604	218,268
Total debt	575,570	610,941
Current portion of long-term debt	(234,449)	(228,721)
Long-term debt	$341,121	$382,220

Credit Facility

Our credit facility is dated April 18, 2007 and includes two amendments dated April 24, 2009 and February 10, 2010. The principal balance of our euro denominated term loan at June 30, 2011 and December 31, 2010 was €105.8 million and €132.4 million, respectively. Interest rates on the credit facility are based on the respective borrowing's denominated London Interbank Offered Rate (LIBOR) or the Wells Fargo Bank, National Association's prime rate, plus an additional margin subject to our consolidated leverage ratio. The additional interest rate margin was 3.50% at June 30, 2011. Our interest rates were 3.70% for the U.S. dollar denominated and 4.72% for the euro denominated term loans at June 30, 2011. Scheduled amortization of principal payments is 1% per year (0.25% quarterly) with an excess cash flow provision for additional annual principal repayment requirements. The amount of the excess cash flow provision payment varies according to our consolidated leverage ratio. Maturities of the term loans and the multicurrency revolving line of credit are in April 2014 and 2013, respectively. The credit facility is secured by substantially all of the assets of Itron, Inc. and our U.S. domestic operating subsidiaries and includes covenants, which contain certain financial ratios and place restrictions on the incurrence of debt, the payment of dividends, certain investments, incurrence of capital

Table of Contents

expenditures above a set limit, and mergers.

The credit facility includes a multicurrency revolving line of credit, which was increased from $240 million to $315 million on January 20, 2011. The increase was completed under the terms of the credit facility. Prepaid debt fees of $379,000 were capitalized associated with the increase in the credit line. There were no other changes to the credit facility.

At June 30, 2011, there were no borrowings outstanding under the revolving line of credit, and $40.0 million was utilized by outstanding standby letters of credit, resulting in $275.0 million being available for additional borrowings.

We repaid $2.7 million and $55.6 million of the term loans during the three and six months ended June 30, 2011, respectively. Repayments of $21.1 million and $73.9 million were made during the three and six months ended June 30, 2010, respectively. These term loan repayments were made with cash flows from operations and cash on hand. We were in compliance with the debt covenants under the credit facility at June 30, 2011.

Convertible Senior Subordinated Notes

On August 4, 2006, we issued $345 million of 2.50% convertible notes due August 2026. Fixed interest payments are required every six months, in February and August of each year. For each six month period beginning August 2011, contingent interest payments of approximately 0.19% of the average trading price of the convertible notes will be made if certain thresholds are met or events occur, as outlined in the indenture. The convertible notes are registered with the SEC and are generally transferable. Our convertible notes are not considered conventional convertible debt as the number of shares, or cash, to be received by the holders was not fixed at the inception of the obligation. We have concluded that the conversion feature of our convertible notes does not need to be bifurcated from the host contract and accounted for as a freestanding derivative, as the conversion feature is indexed to our own stock and would be classified within stockholders' equity if it were a freestanding instrument.

The convertible notes may be converted at the option of the holder at a conversion rate of 15.3478 shares of our common stock for each $1,000 principal amount of the convertible notes, under the following circumstances, as defined in the indenture:

if the closing sale price per share of our common stock exceeds $78.19, which is 120% of the conversion price of $65.16, for at least 20 trading days in the 30 consecutive trading day period ending on the last trading day of the preceding fiscal quarter;

between July 1, 2011 and August 1, 2011, and any time after August 1, 2024;

during the five business days after any five consecutive trading day period in which the trading price of the convertible notes for each day was less than 98% of the average conversion value of the convertible notes;

if the convertible notes are called for redemption;

if a fundamental change occurs; or

upon the occurrence of defined corporate events.

The amount payable upon conversion is the result of a formula based on the closing prices of our common stock for 20 consecutive trading days following the date of the conversion notice. Based on the conversion ratio of 15.3478 shares per $1,000 principal amount of the convertible notes, if our stock price is lower than the conversion price of $65.16, the amount payable will be less than the $1,000 principal amount and will be settled in cash. Our closing stock price at June 30, 2011 was $48.16 per share.

Upon conversion, the principal amount of the convertible notes will be settled in cash and, at our option, the remaining conversion obligation (stock price in excess of conversion price) may be settled in cash, shares, or a combination. The conversion rate for the convertible notes is subject to adjustment upon the occurrence of certain corporate events, as defined in the indenture, to ensure that the economic rights of the convertible note holders are preserved.

The convertible notes also contain purchase options, at the option of the holders, which if exercised would require us to repurchase all or a portion of the convertible notes on August 1, 2011, August 1, 2016, and August 1, 2021 at 100%

of the principal amount, plus accrued and unpaid interest. If we are required to purchase the convertible notes at 100% of the principal amount, no gain or loss would be recognized upon derecognition as the fair value of the consideration transferred to the holder would equal the fair value of the liability component.

On or after August 1, 2011, we have the option to redeem all or a portion of the convertible notes at a redemption price equal to 100% of the principal amount plus accrued and unpaid interest. If we elect to redeem all or a portion of the convertible notes at 100% of the principal amount, no gain or loss would be recognized upon derecognition as the fair value of the consideration transferred to the holder would equal the fair value of the liability component.

The convertible notes are unsecured, subordinated to our credit facility (senior secured borrowings), and are guaranteed by one

Table of Contents

U.S. subsidiary, which is 100% owned. The convertible notes contain covenants, which place restrictions on the incurrence of debt and certain mergers. We were in compliance with these debt covenants at June 30, 2011.
The convertible notes are classified as current on the Consolidated Balance Sheet due to the combination of put, call, and conversion options occurring in 2011.

Our convertible notes are separated between the liability and equity components using our estimated non-convertible debt borrowing rate at the time our convertible notes were issued, which was determined to be 7.38%. This rate also reflects the effective interest rate on the liability component. The equity component would be retained as a permanent component of our shareholders' equity in the event the convertible notes are either purchased or redeemed at 100% of the principal amount. At June 30, 2011, the discount on the liability component was fully amortized. The carrying amounts of the debt and equity components are as follows:

	June 30, 2011	December 31, 2010
	(in thousands)	
Face value of convertible notes	$223,604	$223,604
Unamortized discount	—	(5,336)
Net carrying amount of debt component	$223,604	$218,268
Carrying amount of equity component	$31,831	$31,831

The interest expense relating to both the contractual interest coupon and amortization of the discount on the liability component are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in thousands)			
Contractual interest coupon	$1,397	$1,397	$2,795	$2,795
Amortization of the discount on the liability component	2,693	2,501	5,336	4,957
Total interest expense on convertible notes	$4,090	$3,898	$8,131	$7,752

Note 7: Derivative Financial Instruments

As part of our risk management strategy, we use derivative instruments to hedge certain foreign currency and interest rate exposures. Refer to Note 1, Note 12, and Note 13 for additional disclosures on our derivative instruments.

The fair values of our derivative instruments are determined using the income approach and significant other observable inputs (also known as “Level 2”), as defined by FASB Accounting Standards Codification (ASC) 820-10-20, Fair Value Measurements. We have used observable market inputs based on the type of derivative and the nature of the underlying instrument. The key inputs used at June 30, 2011 included interest rate yield curves (swap rates and futures) and foreign exchange spot and forward rates, all of which are available in an active market. We have utilized the mid-market pricing convention for these inputs at June 30, 2011. We include the effect of our counterparty credit risk based on current published credit default swap rates when the net fair value of our derivative instruments is in a net asset position. We consider our own nonperformance risk when the net fair value of our derivative instruments is in a net liability position by discounting our derivative liabilities to reflect the potential credit risk to our counterparty through applying a current market indicative credit spread to all cash flows.

Table of Contents

The fair values of our derivative instruments determined using the fair value measurement of significant other observable inputs (Level 2) at June 30, 2011 and December 31, 2010 are as follows:

	Balance Sheet Location	Fair Value June 30, 2011 (in thousands)	December 31, 2010
Asset Derivatives			
Derivatives not designated as hedging instruments under ASC 815-20			
Foreign exchange forward contracts	Other current assets	$171	$63
Liability Derivatives			
Derivatives designated as hedging instruments under ASC 815-20			
Interest rate swap contracts	Other current liabilities	$2,395	$5,845
Interest rate swap contracts	Other long-term obligations	182	975
Euro denominated term loan *	Current portion of debt	4,794	4,402
Euro denominated term loan *	Long-term debt	146,556	169,629
Total derivatives designated as hedging instruments under ASC 815-20		$153,927	$180,851
Derivatives not designated as hedging instruments under ASC 815-20			
Foreign exchange forward contracts	Other current liabilities	$200	$457
Total liability derivatives		$154,127	$181,308

* The euro denominated term loan is a nonderivative financial instrument designated as a hedge of our net investment in international operations. It is recorded at its carrying value in the Consolidated Balance Sheets and is not recorded at fair value.

OCI during the reporting period for our derivative and nonderivative instruments designated as hedging instruments (collectively, hedging instruments), net of tax, was as follows:

	2011 (in thousands)	2010
Net unrealized loss on hedging instruments at January 1,	$(10,034)	$(30,300)
Unrealized gain (loss) on derivative instruments	(164)	(2,542)
Unrealized gain (loss) on a nonderivative net investment hedging instrument	(9,262)	24,352
Realized (gains) losses reclassified into net income (loss)	2,774	4,197
Net unrealized loss on hedging instruments at June 30,	$(16,686)	$(4,293)

Cash Flow Hedges

We are exposed to interest rate risk through our credit facility. We enter into swaps to achieve a fixed rate of interest on the hedged portion of debt in order to increase our ability to forecast interest expense. The objective of these swaps is to protect us from increases in the LIBOR base borrowing rates on our floating rate credit facility. The swaps do not protect us from changes to the applicable margin under our credit facility.

In 2007, we entered into a pay fixed 6.59% receive three-month Euro Interbank Offered Rate (EURIBOR), plus 2%, amortizing interest rate swap to convert a significant portion of our euro denominated variable-rate term loan to fixed-rate debt, plus or minus the variance in the applicable margin from 2%, through December 31, 2012. The cash flow hedge is currently, and is expected to be, highly effective in achieving offsetting cash flows attributable to the hedged risk through the term of the hedge. Consequently, effective changes in the fair value of the interest rate swap are recorded as a component of OCI and are recognized in earnings when the hedged item affects earnings. The amounts paid or received on the hedge are recognized as adjustments to interest expense. The notional amount of the swap is reduced each quarter and was $115.6 million (€80.8 million) and $147.7 million (€112.4 million) as of June 30, 2011 and December 31, 2010, respectively. The amount of net losses expected to be reclassified into earnings in the next 12 months is approximately $2.2 million (€1.5 million), which was based on the Reuters euro swap yield curve as of June 30, 2011.

Our two one-year pay-fixed receive one-month LIBOR interest rate swaps, which each converted $100 million of our U.S. dollar term loan from a floating LIBOR interest rate to fixed interest rates of 2.11% and 2.15%, respectively, expired on June 30, 2011. These swaps did not include the additional interest rate margin applicable to our term debt.

We will continue to monitor and assess our interest rate risk and may institute additional interest rate swaps or other derivative instruments to manage such risk in the future.

The before tax effect of our cash flow derivative instruments on the Consolidated Balance Sheets and the Consolidated Statements of Operations for the three and six months ended June 30 are as follows:

Derivatives in ASC 815-20 Cash Flow Hedging Relationships	Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)		Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)			Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)		
			Location	Amount		Location	Amount	
	2011	2010		2011	2010		2011	2010
	(in thousands)			(in thousands)			(in thousands)	
Three Months Ended June 30,								
Interest rate swap contracts	$ (2,149)	$ (839)	Interest expense	$ (1,788)	$ (3,238)	Interest expense	$ (31)	$ (14)
Six Months Ended June 30,								
Interest rate swap contracts	$ (4,477)	$ (4,122)	Interest expense	$ (4,171)	$ (6,810)	Interest expense	$ (80)	$ (74)

Net Investment Hedge

We are exposed to foreign exchange risk through our international subsidiaries. As a result of our acquisition of an international company in 2007, we entered into a euro denominated term loan, which exposes us to fluctuations in the euro foreign exchange rate. Therefore, we have designated this foreign currency denominated term loan as a hedge of our net investment in international operations. The non-functional currency term loan is revalued into U.S. dollars at each balance sheet date, and the changes in value associated with currency fluctuations are recorded as adjustments to long-term debt with offsetting gains and losses recorded in OCI. The notional amount of the term loan declines each quarter due to repayments and was $151.4 million (€105.8 million) and $174.0 million (€132.4 million) as of June 30, 2011 and December 31, 2010, respectively. We had no hedge ineffectiveness.

The before tax and net of tax effects of our net investment hedge nonderivative financial instrument on OCI for the three and six months ended June 30 are as follows:

Nonderivative Financial Instruments in ASC 815-20 Net Investment Hedging Relationships	Euro Denominated Term Loan Designated as a Hedge of Our Net Investment in International Operations

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in thousands)			
Gain (loss) recognized in OCI on derivative (Effective Portion)				
Before tax	$(2,343)	$20,943	$(14,923)	$39,498
Net of tax	$(1,452)	$12,908	$(9,262)	$24,352

Derivatives Not Designated as Hedging Relationships

We are also exposed to foreign exchange risk when we enter into non-functional currency transactions, both intercompany and third-party. At each period-end, foreign currency monetary assets and liabilities are revalued with the change recorded to other income and expense. We enter into monthly foreign exchange forward contracts (a total of 257 contracts were entered into during the six months ended June 30, 2011), not designated for hedge accounting, with the intent to reduce earnings volatility associated with certain of these balances. The notional amounts of the contracts ranged from $50,000 to $72 million, offsetting our exposures from the euro, British pound, Canadian dollar, Czech koruna, Hungarian forint, and various other currencies.

Table of Contents

The effect of our foreign exchange forward derivative instruments on the Consolidated Statements of Operations for the three and six months ended June 30 is as follows:

Derivatives Not Designated as Hedging Instrument under ASC 815-20	Gain (Loss) Recognized on Derivatives in Other Income (Expense)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in thousands)			
Foreign exchange forward contracts	$(1,259)	$3,316	$(3,341)	$3,047

Note 8: Defined Benefit Pension Plans

We sponsor both funded and unfunded defined benefit pension plans for our international employees, primarily in Germany, France, Italy, Indonesia, and Spain, offering death and disability, retirement, and special termination benefits. The defined benefit obligation is calculated annually by using the projected unit credit method. The measurement date for the pension plans was December 31, 2010.

Our defined benefit pension plans are denominated in the functional currencies of the respective countries in which the plans are sponsored; therefore, the balances increase or decrease, with a corresponding change in OCI, due to changes in foreign currency exchange rates. Amounts recognized on the Consolidated Balance Sheets consist of:

	June 30, 2011	December 31, 2010
	(in thousands)	
Plan assets in other long term assets	$(468)	$(412)
Current portion of pension plan liability in wages and benefits payable	2,910	2,656
Long-term portion of pension plan liability	69,675	61,450
Net pension plan benefit liability	$72,117	$63,694

Our asset investment strategy focuses on maintaining a portfolio using primarily insurance funds, which are accounted for as investments and measured at fair value, in order to achieve our long-term investment objectives on a risk adjusted basis. Our general funding policy for these qualified pension plans is to contribute amounts sufficient to satisfy regulatory funding standards of the respective countries for each plan. We contributed $37,000 and $391,000 to the defined benefit pension plans for the three and six months ended June 30, 2011, and $313,000 and $338,000 for the three and six months ended June 30, 2010, respectively. The timing of when contributions are made can vary by plan and from year to year. For 2011, assuming that actual plan asset returns are consistent with our expected rate of return, and that interest rates remain constant, we expect to contribute approximately $500,000 to our defined benefit pension plans. We contributed $519,000 to the defined benefit pension plans for the year ended December 31, 2010.

Net periodic pension benefit costs for our plans include the following components:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in thousands)			
Service cost	$601	475	$1,218	$1,000
Interest cost	969	844	1,886	1,750
Expected return on plan assets	(83)	(71)	(163)	(148)
Amortization of actuarial net loss (gain)	14	(6)	28	(13)
Amortization of unrecognized prior service costs	19	—	37	—
Net periodic benefit cost	$1,520	$1,242	$3,006	$2,589

Table of Contents

Note 9: Stock-Based Compensation

We record stock-based compensation expense for awards of stock options, stock sold pursuant to our ESPP, and the issuance of restricted stock units and unrestricted stock awards. We expense stock-based compensation primarily using the straight-line method over the vesting requirement period. For the three and six months ended June 30, stock-based compensation expense and the related tax benefit were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in thousands)			
Stock options	$511	$952	$1,544	$2,295
Restricted stock units	3,853	3,441	7,404	6,382
Unrestricted stock awards	15	14	190	189
ESPP	164	138	380	255
Total stock-based compensation	$4,543	$4,545	$9,518	$9,121
Related tax benefit	$1,257	$1,324	$2,659	$2,732

We issue new shares of common stock upon the exercise of stock options or when vesting conditions on restricted stock units are fully satisfied.

The fair values of stock options granted were estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	Employee Stock Options			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2011[1]	2010[1]	2011	2010
Dividend yield	—	—	—	—
Expected volatility	—			