SABRE HOLDINGS CORP
Form 10-Q
May 05, 2006

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

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For the Quarterly Period Ended March 31, 2006.

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 1-12175.

SABRE HOLDINGS CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**75-2662240**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3150 Sabre Drive, Southlake, Texas	**76092**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code **(682) 605-1000**

Not Applicable
(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 periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check One):

Large Accelerated Filer ý Accelerated Filer o Non-accelerated Filer o

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	**Outstanding at April 30, 2006**
Class A Common Stock, $.01 par value	132,746,607 Shares

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SABRE HOLDINGS CORPORATION

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SABRE HOLDINGS CORPORATION
CONSOLIDATED BALANCE SHEETS
(In thousands)

	March 31, 2006	December 31, 2005
	(Unaudited)	
Assets		
Current assets		
Cash	$ 195,860	$ 135,233
Restricted cash	9,790	57,019
Marketable securities	152,971	376,585
Accounts receivable, net	569,714	487,034
Prepaid expenses	40,682	41,632
Deferred income taxes	23,282	23,013
Other receivables	138,604	127,772
Total current assets	1,130,903	1,248,288
Property and equipment		
Buildings and leasehold improvements	319,500	318,880
Furniture, fixtures and equipment	39,220	38,349
Computer equipment	159,649	148,965
Internally developed software	274,156	257,990
	792,525	764,184
Less accumulated depreciation and amortization	(360,839)	(334,616)
Total property and equipment	431,686	429,568
Deferred income taxes	19,784	32,419
Investments in joint ventures	158,005	156,277
Goodwill and intangible assets, net	2,367,818	2,333,140
Other assets, net	176,429	174,419
Total assets	$ 4,284,625	$ 4,374,111
Liabilities and stockholders' equity		
Current liabilities		
Accounts payable	$ 179,682	$ 203,663
Travel supplier liabilities and deferred revenue	458,759	301,377
Accrued compensation and related benefits	37,078	74,628
Accrued subscriber incentives	118,072	81,877
Deferred revenues	56,932	32,047
Other accrued liabilities	380,027	398,871
Bridge Facility		800,000
Total current liabilities	1,230,550	1,892,463
Pensions and other postretirement benefits	187,755	191,453
Other liabilities	30,874	23,568

	March 31, 2006	December 31, 2005
Minority interests	6,944	38,948
Long-term capital lease obligation	155,259	158,188
Public and other notes payable	998,540	426,379
Commitments and contingencies		
Stockholders' equity		
Preferred stock: $0.01 par value; 20,000 shares authorized; no shares issued		
Class A Common Stock: $0.01 par value; 250,000 shares authorized; 145,856 shares issued at March 31, 2006 and December 31, 2005	1,459	1,459
Additional paid-in capital	1,265,589	1,275,836
Retained earnings	772,919	769,231
Accumulated other comprehensive loss	(63,660)	(77,872)
Less treasury stock at cost: 13,099 and 14,281 shares, respectively	(301,604)	(325,542)
Total stockholders' equity	1,674,703	1,643,112
Total liabilities and stockholders' equity	$ 4,284,625	$ 4,374,111

See Notes to Consolidated Financial Statements.

SABRE HOLDINGS CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited) (In thousands, except per share amounts)

	Three Months Ended March 31,	
	2006	**2005**
Revenues	$ 700,188	$ 581,888
Cost of revenues	433,776	338,023
Amortization of purchased technology	8,680	2,095
Total cost of revenues	442,456	340,118
Gross Profit	257,732	241,770
Other operating expenses		
Selling, general and administrative	209,883	164,643
Amortization of other intangible assets	9,923	5,933
Total other operating expenses	219,806	170,576
Operating income	37,926	71,194
Other income (expense)		
Interest income	3,979	4,369
Interest expense	(19,766)	(7,614)
Gain on sale of investment		20,594
Other, net	4,585	609
Total other income (expense)	(11,202)	17,958
Income before provision for income taxes	26,724	89,152
Provision for income taxes	9,917	31,471
Net earnings	$ 16,807	$ 57,681
Earnings per common share		
Basic	$ 0.13	$ 0.44
Diluted	$ 0.13	$ 0.44
Weighted average common shares outstanding		
Basic	130,315	130,253
Diluted	132,627	130,753

See Notes to Consolidated Financial Statements.

SABRE HOLDINGS CORPORATION
CONSOLIDATED CONDENSED STATEMENT OF STOCKHOLDERS' EQUITY
THREE MONTHS ENDED MARCH 31, 2006
(Unaudited) (In thousands)

	Class A Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total
Balance at December 31, 2005	$ 1,459	$ 1,275,836	$ 769,231	$ (77,872)	$ (325,542)	$ 1,643,112
Issuances pursuant to:						
Stock option plans		(1,495)			10,458	8,963
Restricted stock (net of forfeitures)		(16,883)			16,883	
Restricted stock withheld upon vesting					(3,538)	(3,538)
Employee stock purchase plan		(1)			135	134
Tax benefit from exercise of employee stock options and restricted stock		1,705				1,705
Dividends, $0.10 per common share			(13,119)			(13,119)
Amortization of stock-based compensation		6,417				6,417
Comprehensive income:						
Net earnings			16,807			16,807
Unrealized gain on foreign currency forward and option contracts, net of deferred income taxes				2,349		2,349
Unrecognized gain on hedge settlement				2,510		2,510
Unrealized gain on investments, net of deferred income taxes				1,109		1,109
Unrealized foreign currency translation gain, net of deferred income taxes				8,244		8,244
Total comprehensive income						31,019
Other		10				10
Balance at March 31, 2006	$ 1,459	$ 1,265,589	$ 772,919	$ (63,660)	$ (301,604)	$ 1,674,703

See Notes to Consolidated Financial Statements.

SABRE HOLDINGS CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited) (In thousands)

	Three Months Ended March 31,	
	2006	**2005**
Operating Activities		
Net earnings	$ 16,807	$ 57,681
Adjustments to reconcile net earnings to cash provided by operating activities:		
Depreciation and amortization	43,122	27,135
Stock-based compensation for employees	6,417	2,675
Allowance for doubtful accounts	4,006	2,070
Deferred income taxes	7,764	(12,286)
Joint venture equity loss (income)	(1,790)	3,968
Gain on sale of investment		(20,594)
Other	(252)	(2,794)
Changes in operating assets and liabilities:		
Accounts and other receivables	(108,899)	(96,402)
Prepaid expenses	(128)	(1,901)
Other assets	6,965	(16,765)
Accrued compensation and related benefits	(37,550)	(31,264)
Accounts payable and other accrued liabilities	180,544	128,560
Pensions and other postretirement benefits	(3,698)	
Excess tax benefits from stock-based compensation arrangements	(638)	
Cash provided by operating activities	112,670	40,083
Investing Activities		
Additions to property and equipment	(27,646)	(17,184)
Purchases of marketable securities	(3,808,308)	(2,668,962)
Sales of marketable securities	4,031,855	2,771,430
Proceeds from sale of investment		26,013
Acquisitions (net of cash acquired)	(54,308)	(61,022)
Proceeds from release of restricted cash	37,211	
Other investing activities	5,886	(12,538)
Cash provided by investing activities	184,690	37,737
Financing Activities		
Proceeds from issuance of Common Stock	5,559	2,691
Dividends paid	(13,119)	(11,894)
Prepayment of Bridge Facility	(800,000)	
Proceeds from borrowings on revolving credit agreement	180,000	
Proceeds from issuance of Notes	397,136	
Excess tax benefits from stock-based compensation arrangements	638	
Purchases of treasury stock		(63,213)
Other financing activities	(7,979)	(72)
Cash used for financing activities	(237,765)	(72,488)
Effect of exchange rate changes on cash and cash equivalents	1,032	(982)
Increase in cash	60,627	4,350
Cash at beginning of period	135,233	49,671
Cash at end of period	$ 195,860	$ 54,021

	Three Months Ended March 31,	

See Notes to Consolidated Financial Statements.

SABRE HOLDINGS CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. General Information

Sabre Holdings Corporation ("Sabre Holdings") is a Delaware holding company. Sabre Inc. is the principal operating subsidiary and sole direct subsidiary of Sabre Holdings. Sabre Inc. or its direct or indirect subsidiaries conduct all of our businesses. In this Quarterly Report on Form 10-Q, references to the "company", "we", "our", "ours" and "us" refer to Sabre Holdings and its consolidated subsidiaries unless otherwise stated or the context otherwise requires.

We are a world leader in travel commerce, marketing travel products and providing distribution and technology solutions for the travel industry. Through our *Sabre*®[1] global distribution system (the "*Sabre* system" or "*Sabre* GDS") subscribers, generally travel agencies, can access information about, and can book reservations for, among other things, airline trips, hotel stays, car rentals, cruises and tour packages. Our *Sabre Travel Network* business operates the *Sabre* GDS. We market and distribute travel related products and services directly to leisure and business travelers including air, hotel, car rental, cruises and packaged trip offerings through our *Travelocity*® business. In addition, our *Sabre Airline Solutions*® business is a leading provider of technology and services, including development and consulting services, to airlines and other travel providers.

2. Summary of Significant Accounting Policies

Basis of Presentation The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles ("GAAP") in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP in the United States for complete financial statements. In the opinion of management, these financial statements contain all adjustments, consisting of normal recurring accruals, necessary to present fairly the financial position, results of operations and cash flows for the periods indicated. The preparation of financial statements in accordance with GAAP in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Operating results for the three months ended March 31, 2006 are not necessarily indicative of results that may be expected for any other interim period or for the year ended December 31, 2006. Our quarterly financial data should be read in conjunction with our Consolidated Financial Statements for the year ended December 31, 2005 (including the notes thereto), set forth in Sabre Holdings Corporation's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 8, 2006.

We consolidate all of our majority-owned subsidiaries and companies over which we exercise control through majority voting rights. From November 7, 2005 through January 23, 2006, we were the primary beneficiary of Zuji Holdings Limited ("Zuji") and consolidated its results, which were previously accounted for using the equity method, in accordance with Financial Accounting Standards Board ("FASB") Interpretation No. 46R, *Consolidation of Variable Interest Entities (Revised)* ("FIN 46R"). In 2005, Travelocity entered into a put option agreement with the other owners of Zuji, exercisable from January 1, 2006 through January 31, 2006. This put option was exercised on January 24, 2006 and Travelocity gained 100% control of Zuji. See Note 3 for additional information. Other than Zuji for the time period noted above, no other entities are currently consolidated due to control through operating agreements, financing agreements, or as the primary beneficiary of a variable interest entity.

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[1] Hotel Spotlight, GetThere, Jurni Network, lastminute.com, Nexion, PromoSpots, reisefeber Sabre, Sabre Airline Solutions, Sabre Holdings, the Sabre Holdings logo, Sabre Travel Network, Surround, Showtickets.com, Site 59, Site59.com, SynXis, TotalTrip, TRAMS, Travelocity, Travelocity Business, Travelocity.com, Zuji are trademarks and/or service marks of an affiliate of Sabre Holdings Corporation. All other trademarks, service marks, or tradenames are the property of their respective owners.

The Consolidated Financial Statements include our accounts after elimination of all significant intersegment balances and transactions. We account for our interests in joint ventures and investments in common stock of other companies that we do not control but over which we exert significant influence using the equity method, with our share of their results classified as revenues. Investments in the common stock of other companies over which we do not exert significant influence are accounted for at cost. We periodically evaluate equity and debt investments in entities accounted for at cost for impairment by reviewing updated financial information provided by the investee, including valuation information from new financing transactions by the investee and information relating to competitors of investees when available. If we determine that a cost method investment is other than temporarily impaired, the carrying value of the investment is reduced to its estimated fair value. To date, writedowns of investments carried at cost have been insignificant to our results of operations.

Reclassifications Certain reclassifications have been made to the 2005 Consolidated Financial Statements to conform to the 2006 presentation. These reclassifications are not material, either individually or in the aggregate, to our financial statements.

Recent Accounting Pronouncements On January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123 (Revised 2004), *Share-Based Payments.* See Note 5 for additional information.

In May 2005, the FASB issued Statement of Financial Accounting Standards No. 154, *Accounting Changes and Error Corrections*, a replacement of APB Opinion No. 20, *Accounting Changes*, and Statement of Financial Accounting Standards No. 3, *Reporting Accounting Changes in Interim Financial Statements*. The standard requires changing the accounting and reporting requirements of voluntary and mandatory (unless the pronouncement provides other transition requirements) changes in accounting principle by requiring retroactive application of the change in accounting principle to prior periods' financial statements, unless it is not practical to do so, rather than recording a cumulative catch up adjustment in net earnings in the year of the change. Reporting error corrections will be handled similar to a change in accounting principles. The standard was effective on January 1, 2006.

Changes in Estimates Sabre Travel Network pays incentive payments to our subscribers, generally travel agents, based upon volume and rates contained within the travel agency contracts. For our larger subscribers, we have always accrued the incentive expense as these volumes represented the majority of our incentive liability. In the first quarter of 2006, we revised our estimate of the incentive liability to include expense associated with our smaller travel agency customers that were previously recorded as payments were made. The incentives from these smaller agencies were immaterial in the past; however, recent analysis of smaller travel agencies showed a pattern of growth in incentives paid. This new accrual methodology resulted in an additional $21 million in incentive expense this quarter. We performed a similar analysis on revenues we received from smaller travel agencies which resulted in an accrual of $7 million in subscriber revenues. Both of these accruals resulted in a net reduction to our after tax net earnings of approximately $9 million or $0.07 per dilutive common share.

Sabre Travel Network has a booking fee cancellation reserve that is calculated at each period end based on historical cancellation rates. In estimating the amount of future cancellations that will require us to refund a booking fee, we assume that a certain percentage of cancellations are followed immediately by a new reservation, without loss of revenue. This assumption is based on historical rates of cancellations that results in new reservations and has a significant impact on the amount reserved. In the first quarter of 2006, our estimate of the rebook rate has increased. This change in the rebook rate assumption lowers the amount of reserve needed for cancelled bookings. The new estimated rate resulted in a $7 million decrease in the booking fee cancellation reserve from what it would have been using the previous rebook assumption resulting in a $4 million increase to after tax net earnings or $0.03 per dilutive common share.

Earnings Per Share Basic earnings per share excludes any dilutive effect of options, warrants and other stock-based awards. The number of shares used in the diluted earnings per share calculations includes the dilutive effect of stock options and restricted shares.

The following table reconciles weighted-average shares used in computing basic and diluted earnings per common share (in thousands):

	Three Months Ended March 31,	
	2006	**2005**
Denominator for basic earnings per common share weighted-average shares	130,315	130,253
Dilutive effect of stock awards and options	2,312	500
Denominator for diluted earnings per common share adjusted weighted-average shares	132,627	130,753

The increase in dilutive shares for the three months ended March 31, 2006 as compared to the same three month period in 2005 is due to a higher market price of our Class A Common Stock, par value $0.01 per share ("Common Stock") and includes the dilutive impact of approximately 3,400,000 options that were issued to US Airways Group, Inc. in 1998 and expire in 2013. Options to purchase approximately 13,739,603 and 18,828,873 weighted-average shares of our Common Stock were outstanding at March 31, 2006 and 2005, respectively, but were excluded from the computation of diluted earnings per share because the effect would be antidilutive.

Restricted Cash At March 31, 2006, we held $10 million in cash that was restricted. Approximately $7 million of this restricted cash is from our consolidation of Zuji and represents bank guarantees required by airlines and other travel regulatory bodies as well as an office premise. At December 31, 2005, we held $57 million in cash that was restricted. $40 million was restricted to fulfill bonding requirements in Europe related to the lastminute.com acquisition. In the first quarter of 2006, $3 million of this restricted cash continued to be restricted and the remaining $37 million was released as a result of a guarantee issued in March 2006 by Sabre Holdings. Additionally, during the first quarter of 2006, we were able to release $11 million in cash held in an escrow account established to fulfill the requirements of a bank guarantee.

3. Significant Events

Legal Settlement We had previously disclosed two lawsuits, which were consolidated in federal court in Fort Worth, Texas, to which we were a party against Northwest Airlines, Inc. ("Northwest") related to Northwest's August 24, 2004 announcement and implementation on September 1, 2004 of a fare supplement for travel reservation bookings made through a GDS, including the *Sabre* GDS, by traditional travel agencies and some online travel sites, such as Travelocity. The bankruptcy court approved a settlement of this litigation by an order effective on February 25, 2006. The settlement resulted in a pre-tax loss of $15 million in the fourth quarter of 2005 recorded in other, net on the Consolidated Statement of Income.

AOL Agreement In 1999, we entered into an agreement with America Online, Inc. ("AOL") that provided, among other things, that Travelocity would be the exclusive reservations engine for AOL. On January 21, 2004, we revised the terms of and extended our agreement with AOL through March 2006. In March 2006, we again extended the terms and now have an agreement through March 2009 which includes an option to exit the contract in March 2008. Under the terms of the extension, Travelocity will have lower fixed payment obligations. We also maintained terms that reduce the fixed payment if AOL doesn't meet revenue targets. This payment is currently estimated to be $12 million over the term of the agreement. Other fixed financial commitments include $6 million to be paid over the term of the agreement. Travelocity continues to be the exclusive reservations engine for AOL's Internet properties under the revised agreement. The revised terms also allow AOL to continue and expand in the travel search arena through its sites and partners. The unamortized portion of fixed payments paid under the original and amended contracts are being expensed on a straight-line basis over the remaining term of the agreement, with $6 million recognized in the first quarter of 2006.

Yahoo! Agreement We have an agreement with Yahoo! whereby we are the exclusive air, car and hotel booking engine on Yahoo! Travel. In March 2006, Yahoo! exercised an option to extend our agreement with them to December 31, 2007 with the same terms as 2006. Payments to Yahoo! are being amortized on a straight-line basis over the remaining term of the agreement.

Long-Term Full Content Agreements In October 2002, we began marketing long-term full content agreements, also known as DCA-3 year agreements, to airlines. Airlines that selected this option under their *Sabre* GDS participating carrier agreements received a discount of approximately 12.5% from the applicable 2003 rates, and were locked into that booking fee rate for three years. Through the long-term full content agreements, participating airlines agreed to commit to the highest level of participation in the Sabre system for three years. As a consequence, we believe that the participation of carriers in the program may have helped to slow the shift of bookings away from the *Sabre* GDS to supplier-controlled outlets.

Many of the original long-term full content agreement contracts are up for renewal in 2006. Sabre Travel Network already has successfully signed new long-term full content agreements with several large U.S. airlines: Delta Airlines, Northwest Airlines, United Airlines and US Airways, which had full content contracts, and AirTran Airways, which did not have a long-term full content contract. The US Airways agreement also includes America West, which did not have a long-term full content contract. The new agreements are for five to seven years and, like the original DCA 3-year agreements, require participating airlines to provide all *Sabre* GDS users broad access to schedules, seat availability and published fares, including Web fares and other promotional fares. These agreements also generally require participating airlines to furnish to passengers booked through the *Sabre* GDS the same customer perquisites and amenities as those afforded to passengers through other GDSs and websites.

Additionally, we have transitioned many carriers from our traditional Participating Carrier Agreement to a new Travel Marketing Agreement that better aligns price with value for the airline and provides better content guarantees to Sabre Travel Network.

Acquisition of TRAMS, Inc. and Related Assets On February 10, 2006, we acquired certain assets from an individual, including all of the outstanding stock of TRAMS, Inc., ("TRAMS") a leading provider of financial reporting, customer relationship management tools and direct marketing solutions and services for travel agencies. The purchase price was $22 million in cash, $20 million of which had been paid as of March 31, 2006. We are also contingently liable for up to $8 million in purchase price if certain contractually determined performance measures are met over the next three years. The acquisition enables Sabre Travel Network to directly serve the end-to-end needs, from front to back-office, of a broad spectrum of travel agencies, with initial focus on small and mid-sized leisure agencies. With the acquisition, Sabre Travel Network will be able to integrate the *TRAMS* offerings more seamlessly with existing and future *Sabre* solutions. The results of operations of TRAMS have been included in our Consolidated Statement of Income and the results of operations of our Sabre Travel Network segment from the date of acquisition. Assets acquired and liabilities assumed have been recorded at their estimated fair values, and the $6 million excess of cost over the estimated fair value of the net assets has been recorded as goodwill. A portion of the acquired goodwill is deductible for tax purposes. The fair values were determined based on preliminary estimates by management and an independent valuation of the net assets acquired, which includes intangible assets of $16 million. Intangible assets subject to amortization are being amortized over a weighted average of 6 years and relate primarily to technology and customer relationships. The final allocation of the purchase price will be based on a complete valuation of all of the assets and liabilities including the outstanding stock of TRAMS and accordingly the information presented on our Consolidated Balance Sheet and elsewhere in this report, is preliminary and may change.

Consolidation and Acquisition of Zuji Holdings Limited On November 7, 2005, pursuant to issuing a $4 million loan to Zuji, we became the primary beneficiary of the joint venture