CERNER CORP /MO/
Form 10-Q
October 29, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended October 2, 2010

OR

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

For the transition period from __________ to __________

Commission File Number 0-15386

CERNER CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	43-1196944
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

2800 Rockcreek Parkway
North Kansas City, Missouri 64117
(816) 201-1024

(Address of Principal Executive Offices, including zip code;
registrant s telephone number, including area code)

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 [ ] (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]

There were 82,852,501 shares of Common Stock, $.01 par value, outstanding at October 21, 2010.

CERNER CORPORATION AND SUBSIDIARIES
I N D E X

Part I. Financial Information
Item 1. Financial Statements
CERNER CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
As of October 2, 2010 (unaudited) and January 2, 2010

(In thousands, except share data)		**2010**		**2009**
Assets				
Current assets:				
Cash and cash equivalents	$	211,747	$	241,723
Short-term investments		353,516		317,113
Receivables, net		463,368		461,411
Inventory		8,058		11,242
Prepaid expenses and other		98,741		106,791
Deferred income taxes		2,285		8,055
Total current assets		1,137,715		1,146,335
Property and equipment, net		500,667		509,178
Software development costs, net		244,852		233,265
Goodwill		161,974		151,479
Intangible assets, net		38,340		33,719
Long-term investments		205,323		-
Other assets		69,512		74,591
Total assets	$	2,358,383	$	2,148,567
Liabilities and Stockholders Equity				
Current liabilities:				
Accounts payable	$	56,671	$	36,893
Current installments of long-term debt		25,751		25,014
Deferred revenue		117,847		137,095
Accrued payroll and tax withholdings		78,072		80,093
Other accrued expenses		46,593		79,008
Total current liabilities		324,934		358,103
Long-term debt		93,282		95,506
Deferred income taxes and other liabilities		112,228		98,372
Deferred revenue		18,578		15,788
Total liabilities		549,022		567,769

Stockholders Equity:				
Cerner Corporation stockholders equity:				
Common stock, $.01 par value, 150,000,000 shares authorized, 83,598,209 shares issued at October 2, 2010 and 82,564,708 shares issued at January 2, 2010		836		826
Additional paid-in capital		618,318		557,545
Retained earnings		1,220,198		1,053,563
Treasury stock		(28,002)		(28,002)
Accumulated other comprehensive loss, net		(2,109)		(3,254)
Total Cerner Corporation stockholders equity		1,809,241		1,580,678
Noncontrolling interest		120		120
Total stockholders equity		1,809,361		1,580,798
Total liabilities and stockholders equity	$	2,358,383	$	2,148,567

See notes to condensed consolidated financial statements (unaudited).

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CERNER CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
For the three and nine months ended October 2, 2010 and October 3, 2009
(unaudited)

	Three Months Ended		Nine Months Ended	
(In thousands, except per share data)	**2010**	**2009**	**2010**	**2009**
Revenues:				
System sales	$ 133,439	$ 118,325	$ 386,292	$ 332,816
Support, maintenance and services	321,289	284,189	939,909	849,461
Reimbursed travel	7,955	6,901	23,820	23,266
Total revenues	462,683	409,415	1,350,021	1,205,543
Costs and expenses:				
Cost of system sales	57,396	47,934	155,087	132,127
Cost of support, maintenance and services	13,797	14,644	46,536	46,506
Cost of reimbursed travel	7,955	6,901	23,820	23,266
Sales and client service	189,320	171,415	566,943	516,401
Software development (includes amortization of $17,756 and $50,015 for the three and nine months ended October 2, 2010; and $16,922 and $45,801 for the three and nine months ended October 3, 2009.)	67,257	66,752	202,024	196,578
General and administrative	32,966	31,059	99,611	91,819
Total costs and expenses	368,691	338,705	1,094,021	1,006,697
Operating earnings	93,992	70,710	256,000	198,846
Other income (expense):				
Interest income (expense), net	87	180	2,291	(287)
Other income (expense), net	5	(3)	(566)	414
Total other income (expense), net	92	177	1,725	127
Earnings before income taxes	94,084	70,887	257,725	198,973
Income taxes	(33,212)	(22,493)	(91,090)	(66,004)

Net earnings	$	60,872	$	48,394	$	166,635	$	132,969
Basic earnings per share	$	0.74	$	0.60	$	2.03	$	1.65
Diluted earnings per share	$	0.71	$	0.57	$	1.95	$	1.59
Basic weighted average shares outstanding		82,547		81,225		82,279		80,750
Diluted weighted average shares outstanding		85,360		84,172		85,273		83,576

See notes to condensed consolidated financial statements (unaudited).

CERNER CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the nine months ended October 2, 2010 and October 3, 2009
(unaudited)

(In thousands)	Nine Months Ended 2010	Nine Months Ended 2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	$ 166,635	$ 132,969
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	140,871	137,620
Share-based compensation expense	17,050	11,491
Provision for deferred income taxes	18,802	7,864
Changes in assets and liabilities (net of businesses acquired):		
Receivables, net	(2,915)	7,432
Inventory	3,174	(1,010)
Prepaid expenses and other	16,675	(13,081)
Accounts payable	24,455	(46,264)
Accrued income taxes	(21,393)	(1,962)
Deferred revenue	(14,780)	(8,966)
Other accrued liabilities	(13,877)	13,065
Net cash provided by operating activities	334,697	239,158
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital purchases	(75,341)	(89,863)
Capitalized software development costs	(61,783)	(58,698)
Purchases of investments	(627,904)	(89,176)
Maturities of investments	379,705	75,449
Purchase of other intangibles	(8,034)	(8,916)
Acquisition of businesses, net of cash acquired	(14,486)	(3,529)
Net cash used in investing activities	(407,843)	(174,733)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from sale of future receivables	1,516	1,888
Long-term debt repayments	(2,404)	(7,065)
Proceeds from excess tax benefits from stock compensation	17,884	13,583
Proceeds from exercise of options	23,266	24,637
Net cash provided by financing activities	40,262	33,043

Effect of exchange rate changes on cash		2,908		10
Net (decrease) increase in cash and cash equivalents		(29,976)		97,478
Cash and cash equivalents at beginning of period		241,723		270,494
Cash and cash equivalents at end of period	$	211,747	$	367,972
Supplemental disclosures of cash flow information:				
Cash paid during the year for:				
Interest	$	3,483	$	4,317
Income taxes, net of refund		88,238		40,179
Summary of acquisition transactions:				
Fair value of tangible assets acquired	$	2,126	$	-
Fair value of intangible assets acquired		5,076		-
Fair value of goodwill		11,290		3,529
Fair value of current liabilities assumed		(1,057)		-
Fair value of contingent liability payable		(1,725)		-
Cash paid for acquisition		15,710		3,529
Cash acquired		(1,224)		-
Net cash used	$	14,486	$	3,529

See notes to condensed consolidated financial statements (unaudited).

CERNER CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(1) Interim Statement Presentation

The condensed consolidated financial statements included herein have been prepared by the Company without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations, although we believe that the disclosures are adequate to make the information presented not misleading. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in our latest annual report on Form 10-K.

In our opinion, the accompanying unaudited condensed consolidated financial statements include all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position and the results of operations and cash flows for the periods presented. Our interim results as presented in this Form 10-Q are not necessarily indicative of the operating results for the entire year.

The condensed consolidated financial statements were prepared using accounting principles generally accepted in the United States (GAAP). These principles require us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. Actual results could differ from those estimates.

Certain prior year amounts in the condensed consolidated financial statements have been reclassified to conform to the current year presentation. These reclassifications had no effect on the results of operations or stockholders equity as previously reported.

Our third fiscal quarter ends on the Saturday closest to September 30. The 2010 and 2009 third quarters ended on October 2, 2010 and October 3, 2009, respectively. All references to years in these notes to condensed consolidated financial statements represent the three or nine months ended of the third fiscal quarters, respectively, unless otherwise noted.

Recent Accounting Pronouncements

In July 2010, Accounting Standards Update (ASU) 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, was issued and amends ASC 310, *Receivables*. ASU 2010-20 requires increased disclosures about the credit quality of financing receivables and allowances for credit losses, including disclosure about credit quality indicators, past due information and modifications of financing receivables. Trade accounts receivable with maturities of one year or less are excluded from the disclosure requirements. The guidance is generally effective for reporting periods ending after December 15, 2010. We are currently evaluating the impact the adoption of ASU 2010-20 will have on our consolidated financial statements.

(2) Acquisitions

On January 4, 2010, we completed the purchase of 100% of the outstanding common shares of IMC Health Care, Inc. (IMC), a provider of employer sponsored on-site health centers. The acquisition of IMC expanded our employer health initiatives, such as on-site employer health centers, occupational health services and wellness programs. Consideration for this transaction was $15.7 million in cash plus additional contingent consideration, which is payable if we achieve certain revenue milestones during the fiscal year 2010 from the clients acquired from IMC. We valued the contingent consideration at $1.7 million based on a probability-weighted assessment of potential contingent consideration payment scenarios ranging up to $2.5 million. Based on the third quarter 2010 assessment, we reduced the contingent consideration liability to $0.9 million and recognized a gain of $0.8 million within the Condensed Consolidated Statements of Operations as a component of general and administrative expenses. The allocation of the purchase price to the estimated fair values of the identified tangible and intangible assets acquired, net of liabilities assumed, is summarized below:

(in thousands)

	Allocation Amount
Tangible assets and liabilities	
Current assets	$ 1,862
Property and equipment	264
Current liabilities	(1,057)
Total net tangible assets acquired	1,069
Intangible assets	
Customer relationships	4,073
Non-compete agreements	1,003
Total intangible assets acquired	5,076
Goodwill	11,290
Total purchase price	$ 17,435

The fair values of the acquired intangible assets and the contingent consideration were estimated by applying the income approach. Such estimations required the use of inputs that were unobservable in the market place (Level 3), including a discount rate that we estimated would be used by a market participant in valuing these assets, projections of revenues and cash flows, probability weighting factors and client attrition rates. See Note 3 for further information about the fair value level hierarchy.

The goodwill was allocated to our Domestic operating segment and is expected to be deductible for tax purposes. The other identifiable intangible assets are being amortized over five years. The operating results of IMC were combined with our operating results subsequent to the purchase date of January 4, 2010. Pro-forma results of operations have not been presented because the effect of this acquisition was not material to our results.

(3) Fair Value Measurements

We determine fair value measurements used in our condensed consolidated financial statements based upon the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity s own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs). The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described below:

Level 1 Valuations based on quoted prices in active markets for identical assets or liabilities that the entity has the ability to access.

Level 2 Valuations based on quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable data for substantially the full term of the assets or liabilities.

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

The following table details our financial assets measured at fair value within the fair value hierarchy:

(In thousands)		October 2, 2010			January 2, 2010		
	Balance Sheet	Fair Value Measurements Using			Fair Value Measurements Using		
Description	Classification	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Money market funds	Cash equivalents	$ 20,541	$ -	$ -	$ 80,242	$ -	$ -
Time deposits	Cash equivalents		200	-	-	8,523	-
Corporate bonds	Cash equivalents	-	7,200	-	-	8,194	-
Time deposits	Short-term investments	-	33,817	-	-	37,784	-
Commercial paper	Short-term investments	-	58,500	-	-	19,987	-
Government and corporate bonds	Short-term investments	-	239,949	-	-	164,792	-
Auction rate securities	Short-term investments	-	-	18,465	-	-	85,203
Put-like feature	Short-term investments	-	-	2,785	-	-	9,347
Government and corporate bonds	Long-term investments	-	205,323	-	-	-	-

Our auction rate securities have been classified as Level 3 assets within the fair value hierarchy, as their valuation requires substantial judgment and estimation of factors that are not currently observable in the market due to the lack of trading in the securities. If different assumptions were used for the various inputs to the valuation, including, but not limited to, assumptions involving the estimated holding periods for the auction rate securities, the estimated cash flows over those estimated lives, and the estimated discount rates, including the liquidity discount rate, applied to those cash flows, the estimated fair value of these investments could be significantly higher or lower than the fair value we determined.

The table below presents the activity of our assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3):

	Three Months Ended		Nine Months Ended	
(In thousands)	2010	2009	2010	2009
Beginning balance	$ 30,850	$ 99,150	$ 94,550	$ 105,300
Redemptions at par	(9,600)	(3,900)	(73,300)	(10,050)
Unrealized gain on auction rate securities included in earnings	1,179	1,924	6,866	11,757
Unrealized loss on put-like feature included in earnings	(1,179)	(1,924)	(6,866)	(11,757)
Ending balance	$ 21,250	$ 95,250	$ 21,250	$ 95,250

We classify our long-term, fixed rate debt as a long-term liability on the balance sheet and estimate the fair value using a Level 3 discounted cash flow analysis based on our current borrowing rates for debt with similar maturities. The fair value of our long-term debt, including current maturities, was approximately $130.6 million at October 2, 2010.

(4) Receivables

Receivables consist of accounts receivable and contracts receivable. Accounts receivable represent recorded revenues that have been billed. Contracts receivable represent recorded revenues that are billable by us at future dates under the terms of a contract with a client. Billings and other consideration received on contracts in excess of related revenues recognized are recorded as deferred revenue. Substantially all receivables are derived from sales and related support and maintenance and professional services of our clinical, administrative and financial information systems and solutions to healthcare providers located throughout the United States and in certain non-U.S. countries.

We perform ongoing credit evaluations of our clients and generally do not require collateral from our clients. We provide an allowance for estimated uncollectible accounts based on specific identification, historical experience and our judgment. Provisions for losses on uncollectible accounts for the first nine months of 2010 and 2009 totaled $7.5 million and $2.6 million, respectively. A summary of net receivables is as follows:

(In thousands)	October 2, 2010	January 2, 2010
Gross accounts receivable	$ 345,464	$ 342,992
Less: Allowance for doubtful accounts	18,858	16,895
Accounts receivable, net of allowance	326,606	326,097
Contracts receivable	136,762	135,314
Total receivables, net	$ 463,368	$ 461,411

During the second quarter of 2008, Fujitsu Services Limited s (Fujitsu) contract as the prime contractor in the National Health Service (NHS) initiative to automate clinical processes and digitize medical records in the Southern region of England was terminated by the NHS. This had the effect of automatically terminating our subcontract for the project. We are in dispute with Fujitsu regarding Fujitsu s obligation to pay the amounts comprised of accounts receivable and contracts receivable related to that subcontract, and we are working with Fujitsu to resolve these issues based on processes provided for in the contract. Part of that process requires resolution of disputes between Fujitsu and the NHS regarding the contract termination. As of October 2, 2010, it remains unlikely that the matter will be resolved in the next 12 months. Therefore these receivables have been classified as long-term and represent the significant majority of other long-term assets as of the third quarter ended October 2, 2010. While the ultimate collectability of the receivables pursuant to this process is uncertain, we believe that we have valid and equitable grounds for recovery of such amounts and that collection of recorded amounts is probable.

During the first nine months of 2010 and 2009, we received total client cash collections of $1,402.6 million and $1,304.3 million, respectively, of which $45.8 million and $54.0 million were received from third party arrangements with non-recourse payment assignments.

(5) Income Taxes

We determine the tax provision for interim periods using an estimate of our annual effective tax rate, adjusted for discrete items, if any, that are taken into account in the relevant period. Each quarter we update our estimate of the annual effective tax rate, and if our estimated tax rate changes we make a cumulative adjustment. We classify interest and penalties associated with unrecognized tax benefits as income tax expense in our Condensed Consolidated Statements of Operations.

Our effective tax rate was 35.3% and 33.2% for the first nine months of 2010 and 2009, respectively. This increase is primarily due to the research and development tax credit not being extended for the 2010 tax year and a decrease in unrecognized tax benefits in the third quarter of 2009 as a result of the Internal Revenue Service completion of the 2007 income tax return and refund claim related to the foreign tax credit for the 2004, 2005 and 2006 income tax returns.

During the first quarter of 2010, the Internal Revenue Service commenced its examination of the 2008 income tax return. We do not believe this examination will have a material effect on our financial position, results of operations or liquidity.

Other than the aforementioned matter, we do not anticipate any settlements of the remaining unrecognized tax benefits within the next 12 months.

(6) Earnings Per Share

Basic earnings per share (EPS) excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in our earnings. A reconciliation of the numerators and the denominators of the basic and diluted per share computations are as follows:

	Three Months Ended								
	2010				2009				
(In thousands, except per share data)		Earnings (Numerator)	Shares (Denominator)		Per-Share Amount		Earnings (Numerator)	Shares (Denominator)		Per-Shar Amoun
Basic earnings per share:									
Income available to common stockholders	$	60,872	82,547	$	0.74	$	48,394	81,225	$	0
Effect of dilutive securities:									
Stock options		-	2,813				-	2,947		
Diluted earnings per share:									
Income available to common stockholders including assumed conversions	$	60,872	85,360	$	0.71	$	48,394	84,172	$	0

Options to purchase 0.7 million and 1.2 million shares of common stock at per share prices ranging from $58.21 to $86.70 and $42.92 to $136.86 were outstanding for the three months ended October 2, 2010 and October 3, 2009, respectively, but were not included in the computation of diluted earnings per share because the options were anti-dilutive. In addition, the computation of diluted earnings per share does not include 118,000 performance based non-vested stock awards, as all necessary conditions of such contingently issuable shares have not been satisfied.

	Nine Months Ended								
	2010				2009				
(In thousands, except per share data)		Earnings (Numerator)	Shares (Denominator)		Per-Share Amount		Earnings (Numerator)	Shares (Denominator)	Per-Sl Amo
Basic earnings per share:									
Income available to common stockholders	$	166,635	82,279	$	2.03	$	132,969	80,750	$
Effect of dilutive securities:									
Stock options		-	2,994				-	2,826	
Diluted earnings per share:									
Income available to common stockholders including assumed conversions	$	166,635	85,273	$	1.95	$	132,969	83,576	$

Options to purchase 0.5 million and 2.1 million shares of common stock at per share prices ranging from $58.21 to $86.70 and $36.72 to $136.86 were outstanding for the nine months ended October 2, 2010 and October 3, 2009, respectively, but were not included in the computation of diluted earnings per share because the options were anti-dilutive. In addition, the computation of diluted earnings per share does not include 118,000 performance based non-vested stock awards, as all necessary conditions of such contingently issuable shares have not been satisfied.

(7) Share-Based Compensation

On March 12, 2010 approximately 115,000 stock options were granted to executive officers and other executive level associates under our Long-Term Incentive Plan F. These awards will vest 40% on March 12, 2012, and 20% will vest on March 12, 2013, 2014 and 2015. The fair value of each of these awards was $44.89 per award. Total compensation expense related to these awards is $5.1 million, which is expected to be recognized over a period of 5 years.

On June 1, 2010 we granted approximately 118,000 shares of performance-based non-vested stock to certain executive officers, pursuant to our Long-Term Incentive Plan F. The fair value of each of these awards was $81.90 based on the closing price of our common stock on the date of grant. These awards will vest according to the following schedule, contingent upon a relative adjusted GAAP earnings growth percentage over 2009 for each respective year and subjective performance criteria for certain shares, as defined in the award agreements:

Vesting Dates	Number of Shares
June 1, 2011	14,000
June 1, 2012	15,500
June 1, 2013	88,500
Total Shares	**118,000**

Approximately 21% of the total shares related to this award were forfeited due to the resignation of an executive officer in the third quarter of 2010. The amount of compensation expense recognized is based on management s estimate of the most likely outcome and will be reassessed at each reporting date through the final vesting date, which may result in adjustments to compensation cost. Based on a current period vesting probability assessment, total compensation cost related to these awards is $7.6 million, net of forfeitures, and is expected to be recognized over a period of 3 years.

The following table presents the total compensation expense recognized in the condensed consolidated statements of operations with respect to stock options, non-vested shares and Associate Stock Purchase Plan shares:

	Three Months Ended		Nine Months Ended	
(In thousands)	2010	2009	2010	2009
Stock option and non-vested share compensation expense	$ 6,244	$ 4,523	$ 17,050	$ 11,485
Associate stock purchase plan expense	424	248	1,229	913
Amounts capitalized in software development costs, net of amortization	(118)	(66)	(376)	(187)
Amounts charged against earnings, before income tax benefit	$ 6,550	$ 4,705	$ 17,903	$ 12,211
Amount of related income tax benefit recognized in earnings	$ 2,440	$ 1,753	$ 6,669	$ 4,549

As of October 2, 2010, there was $55.0 million of total unrecognized compensation cost related to stock options granted under all plans. That cost is expected to be recognized over a weighted-average period of 3.15 years.

(8) Comprehensive Income

Total comprehensive income, which includes net earnings, foreign currency translation adjustments and gains and losses from a hedge of our net investment in the United Kingdom (U.K.), amounted to $80.7 million and $52.8 million for the three months ended October 2, 2010 and October 3, 2009, respectively, and $167.8 million and $142.0 million for the nine months ended October 2, 2010 and October 3, 2009, respectively. None of the items within comprehensive income, including net earnings, relate to non-controlling interests.

As of October 2, 2010, we designated all of our Great Britain Pound (GBP) denominated long-term debt as a net investment hedge of our U.K. operations. The objective of the hedge is to reduce our foreign currency exposure in the U.K. subsidiary investment. Changes in the exchange rate between the United States Dollar (USD) and GBP, related to the notional amount of the hedge, are recognized as a component of accumulated other comprehensive income (loss), to the extent the hedge is effective.

The following tables represent the fair value of the net investment hedge included within the Condensed Consolidated Balance Sheets and the related unrealized gain or loss, net of related income tax effects:

(In thousands)

	Balance Sheet	Fair Value	
		October 2,	January 2,
Derivatives designated	Classification	2010	2010

Net investment hedge	Short-term (S/T) liabilities	$ 14,689	$ 15,015
Net investment hedge	Long-term (L/T) liabilities	73,445	75,075
Total net investment hedge		$ 88,134	$ 90,090

(In thousands)

Derivatives designated	Net Unrealized Gain (Loss) For the Three Months Ended 2010	2009	Net Unrealized Gain (Loss) For the Nine Months Ended 2010	2009
Net investment hedge - S/T	$ (361)	$ 226	$ 204	$ (815)
Net investment hedge - L/T	(1,803)	1,356	1,023	(4,887)
Total net investment hedge	$ (2,164)	$ 1,582	$ 1,227	$ (5,702)

We recognize foreign currency transaction gains and losses within the Condensed Consolidated Statements of Operations as a component of general and administrative expenses. We realized a foreign currency loss of $0.9 million and a gain of $0.03 million during the three months ended October 2, 2010 and October 3, 2009, respectively, and a loss of $0.3 million and a gain of $4.0 million during the nine months ended October 2, 2010 and October 3, 2009, respectively.

(9) Contingencies

The terms of our software license agreements with our clients generally provide for a limited indemnification of such intellectual property against losses, expenses and liabilities arising from third party claims based on alleged infringement by our solutions of an intellectual property right of such third party. The terms of such indemnification often limit the scope of and remedies for such indemnification obligations and generally include a right to replace or modify an infringing solution. To date, we have not had to reimburse any of our clients for any losses related to these indemnification provisions pertaining to third party intellectual property infringement claims. For several reasons, including the lack of prior indemnification claims and the lack of a monetary liability limit for certain infringement cases under the terms of the corresponding agreements with our clients, we cannot determine the maximum amount of potential future payments, if any, related to such indemnification provisions.

From time to time we are involved in routine litigation incidental to the conduct of our business, including for example, employment disputes and litigation alleging solution defects, intellectual property infringement, violations of law and breaches of contract and warranties. We believe that no such routine litigation currently pending against us, if adversely determined, would have a material adverse effect on our consolidated financial position, results of operations or cash flows.

(10) Segment Reporting

We have two operating segments, Domestic and Global. Revenues are derived primarily from the sale of clinical, financial and administrative information systems and solutions. The cost of revenues includes the cost of third party consulting services, computer hardware and sublicensed software purchased from computer and software manufacturers for delivery to clients. It also includes the cost of hardware maintenance and sublicensed software support subcontracted to the manufacturers. Operating expenses incurred by the geographic business segments consist of sales and client service expenses including salaries of sales and client service personnel, communications expenses and unreimbursed travel expenses. Performance of the segments is assessed at the operating earnings level and, therefore, the segment operations have been presented as such. Other includes expenses such as software development, marketing, general and administrative, share-based compensation expense and depreciation that have not been allocated to the operating segments. It is impractical for us to track assets by geographical business segment. Accounting policies for each of the reportable segments are the same as those used on a consolidated basis. The following table presents a summary of the operating information for the three and nine months ended October 2, 2010 and October 3, 2009.

	Operating Segments			
(In thousands)	Domestic	Global	Other	Total
Three months ended 2010				
Revenues	$ 394,052	$ 68,631	$	$ 462,683
Cost of revenues	64,150	14,998		79,148
Operating expenses	102,605	29,482	157,456	289,543
Total costs and expenses	166,755	44,480	157,456	368,691
Operating earnings (loss)	$ 227,297	$ 24,151	$ (157,456)	$ 93,992

	Operating Segments			
(In thousands)	Domestic	Global	Other	Total

Three months ended 2009								
Revenues	$	338,508	$	70,907	$		$	409,415
Cost of revenues		57,759		11,720				69,479
Operating expenses		90,093		32,658		146,475		269,226
Total costs and expenses		147,852		44,378		146,475		338,705
Operating earnings (loss)	$	190,656	$	26,529	$	(146,475)	$	70,710

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	Operating Segments			
(In thousands)	Domestic	Global	Other	Total
Nine months ended 2010				
Revenues	$ 1,130,384	$ 219,637	$	$ 1,350,021
Cost of revenues	189,540	35,903		225,443
Operating expenses	311,663	93,577	463,338	868,578
Total costs and expenses	501,203	129,480	463,338	1,094,021
Operating earnings (loss)	$ 629,181	$ 90,157	$ (463,338)	$ 256,000

	Operating Segments			
(In thousands)	Domestic	Global	Other	Total
Nine months ended 2009				
Revenues	$ 997,441	$ 208,102	$	$ 1,205,543
Cost of revenues	169,567	32,333		201,899
Operating expenses	272,552	97,179	435,067	804,798
Total costs and expenses	442,119	129,512	435,067	1,006,697
Operating earnings (loss)	$ 555,322	$ 78,590	$ (435,067)	$ 198,846

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

The following Management Discussion and Analysis (MD&A) is intended to help the reader understand the results of operations and financial condition of Cerner Corporation (Cerner, the Company, we, us or our). This MD&A is provided as a supplement to, and should be read in conjunction with, our condensed consolidated financial statements and the accompanying notes to the financial statements (Notes) found above.

Our third fiscal quarter ends on the Saturday closest to September 30. The 2010 and 2009 third quarters ended on October 2, 2010 and October 3, 2009, respectively. All references to years in the MD&A represent the respective three or nine months ended of the third fiscal quarters, unless otherwise noted.

Except for the historical information and discussions contained herein, statements contained in this Form 10-Q may constitute forward looking statements within the meaning of Section 21E of the Securities and Exchange Act of 1934, as amended (the Act). Forward-looking statements can often be identified by the use of forward-looking terminology, such as could, should, will, intended, continue, believe, may, expect, hope, anticipate, goal, estimate or the negative of these words, variations thereof or similar expressions. These statements involve a number of risks, uncertainties and other factors that could cause actual results to differ materially, including: the possibility of product-related liabilities; potential claims for system errors and warranties; the possibility of interruption at our data centers or client support facilities; our proprietary technology may be subject to claims for infringement or misappropriation of intellectual property rights of others, or may be infringed or misappropriated by others; risks associated with our non-U.S. operations; risks associated with our ability to effectively hedge exposure to fluctuations in foreign currency exchange rates; the potential for tax legislation initiatives that could adversely affect our tax position and/or challenges to our tax positions in the United States and non-U.S. countries; risks associated with our recruitment and retention of key personnel; risks related to our reliance on third party suppliers; risks inherent with business acquisitions; changing political, economic and regulatory influences; government regulation; significant competition and market changes; risks associated with the ongoing adverse financial market environment and uncertainty in global economic conditions; variations in our quarterly operating results; potential inconsistencies in our sales forecasts compared to actual sales; volatility in the trading price of our common stock; the authority of our Board of Directors to issue preferred stock and anti-takeover provisions contained in our corporate governance documents; and, other risks, uncertainties and factors discussed elsewhere in this Form 10-Q, in our other filings with the Securities and Exchange Commission or in materials incorporated therein by reference. Forward looking statements are not guarantees of future performance or results. We undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes in future operating results, financial condition or business over time.

Management Overview

Our revenues are primarily derived by selling, implementing and supporting software solutions, clinical content, hardware, healthcare devices and services that give healthcare providers secure access to clinical, administrative and financial data in real time, allowing them to improve the quality, safety and efficiency in the delivery of healthcare. We implement the healthcare solutions as stand-alone, combined or enterprise-wide systems. *Cerner Millennium*® software solutions can be managed by our clients or in our data centers via a managed services model.

Our fundamental strategy centers on creating organic growth by investing in research and development (R&D) to create solutions and services for the healthcare industry. This strategy has driven strong growth over the long-term, as reflected in five- and ten-year compound annual revenue growth rates of 13% or more. This growth has also created a very strategic footprint in healthcare, with *Cerner*® solutions licensed by over 8,500 facilities, including approximately 2,300 hospitals; 3,400 physician practices with over 30,000 physicians; 600 ambulatory facilities, such as laboratories, ambulatory centers, cardiac facilities, radiology clinics and surgery centers; 700 home health facilities; and 1,500 retail pharmacies. Selling additional solutions back into this client base is an important element of our future revenue growth. We are also focused on driving growth through market share expansion by replacing competitors in healthcare settings that are looking to replace their current healthcare information technology (HIT) partners or those who have not yet strategically aligned with a supplier.

We expect to drive growth through new initiatives and services that reflect our ongoing ability to innovate and expand our reach into healthcare. Examples of these include our *CareAware*® healthcare device architecture and devices, *Cerner Healthe* employer services, *Cerner ITWorks*℠ services, *Cerner RevWorks*℠ services, physician practice solutions and solutions and services for the pharmaceutical market. Finally, we are focused on selling our solutions and services outside of the United States. Many non-U.S. markets have a low penetration of HIT solutions and their governing bodies are in many cases focused on HIT as part of their strategy to improve the quality and lower the cost of healthcare.

Beyond our strategy for driving revenue growth, we are also focused on earnings growth. Similar to our history of growing revenue, our net earnings have increased at more than 20% compound annual rates over five- and ten-year periods. We believe we can continue driving strong levels of earnings growth while also leveraging key areas to create operating margin expansion. The primary areas of opportunity for margin expansion include:

- becoming more efficient at implementing our software by leveraging implementation tools and methodologies we have developed that can reduce the amount of effort required to implement our software;

- leveraging our investments in R&D by addressing new markets that do not require significant incremental R&D but can contribute significantly to revenue growth; and

- leveraging our scalable business infrastructure to reduce the rate of increase in general and administrative spending to below our revenue growth rate.

We are also focused on increasing cash flow by growing earnings, reducing the use of working capital and controlling capital expenditures.

Healthcare Information Technology Market

Overall, while the weak global economy has impacted and could continue to impact our business, we believe there are several factors that are favorable for the HIT industry. Because HIT solutions play an important role in healthcare by improving safety, efficiency and reducing cost, they are often viewed as more strategic than other potential purchases. Most United States healthcare providers also recognize that they must invest in HIT to meet regulatory, compliance and government reimbursement requirements. In addition, with the Centers for Medicare and Medicaid Services estimating United States healthcare spending at $2.5 trillion or 17.3 percent of 2009 Gross Domestic Product, politicians and policymakers agree that the growing cost of our healthcare system is unsustainable. Leaders of both parties say the intelligent use of information systems will improve health outcomes and, correspondingly, drive down costs. They cite a 2005 study by RAND Corp., which estimated that the widespread adoption of HIT in the United States could cut healthcare costs by $162 billion annually.

In 2009, the broad recognition that HIT is essential to helping control healthcare costs contributed to the inclusion of HIT incentives in the American Recovery and Reinvestment Act (ARRA). The Health Information Technology for Economic and Clinical Health (HITECH) provisions within ARRA include more than $35 billion to incent healthcare organizations to modernize operations through meaningful use of HIT. We believe these incentives will create a period of increased demand for HIT solutions and services in the United States and that Cerner is well positioned to benefit due to our large footprint in United States hospitals and physician practices and our proven ability to deliver value.

Another dynamic in the United States marketplace is the recently passed healthcare reform legislation. We believe the legislation, which promises to drive insurance coverage to an estimated 32 million additional consumers, will have many second order effects on our clients. For example, healthcare providers may face increased volumes that could create capacity constraints, and they may find it challenging to profitably provide care at the rates reimbursed under the expanded coverage models. There will also be additional compliance and reporting challenges for our clients in the area of pay-for-quality and waste, fraud, and abuse measures. We believe these challenges are strong incentives for providers to maximize efficiency and create the need for our clients to further leverage HIT investments, all of which represent a long-term positive for HIT.

Outside of the United States, the economy has impacted and could continue to impact our results in almost all regions. However, we believe long-term revenue growth opportunities outside the United States remain significant because other countries are also grappling with increased healthcare spending, safety concerns and inefficient care, and many of these countries recognize HIT as an important part of the solution to these issues.

In summary, while the current economic environment has impacted our business, the fundamental value proposition of HIT remains strong. The HIT industry will likely benefit as healthcare providers and governments continue to recognize that these solutions and services contribute to safer, more efficient healthcare.

Results Overview

The Company delivered strong levels of bookings, revenues, earnings and cash flows in the third quarter of 2010. New business bookings revenue, which reflects the value of executed contracts for software, hardware and professional services and managed services, was $495.7 million in the third quarter of 2010, which was an increase of 17% compared to $424.3 million in the third quarter of 2009. Revenues for the third quarter of 2010 increased 13% to $462.7 million compared to $409.4 million in the year-ago quarter. The year-over-year increase in revenue in the third quarter reflects improved economic conditions and demand driven by the stimulus incentives.

Third quarter 2010 net earnings were $60.9 million and diluted earnings per share were $0.71. Third quarter 2009 net earnings were $48.4 million and diluted earnings per share were $0.57. Third quarter 2010 and 2009 net earnings and diluted earnings per share reflect the impact of shared-based compensation expense. Share-based compensation expense reduced third quarter 2010 net earnings and diluted earnings per share by $4.1 million and $0.05, respectively, and third quarter 2009 earnings and diluted earnings per share by $3.0 million and $0.04, respectively.

The growth in net earnings and diluted earnings per share was driven primarily by strong revenue growth and continued progress with our margin expansion initiatives, particularly leveraging R&D investments and controlling general and administrative expenses. Our third quarter 2010 operating margin was 20.3%, which is 300 basis points higher than the year-ago quarter and reflects the achievement of our long-term goal of achieving 20% operating margins.

We had strong cash collections of receivables of $471.8 million in the third quarter of 2010 compared to $410.6 million in the third quarter of 2009. Days sales outstanding was 91 days in the third quarter of 2010 compared to 88 days in the second quarter of 2010 and 105 days in the third quarter of 2009. The majority of the year-over-year decline is driven by the reclassification of our Fujitsu receivable to other long term assets during the fourth quarter of 2009, which is not included in our days sales outstanding calculation. Operating cash flows for the third quarter of 2010 were strong at $119.0 million compared to $73.4 million in the third quarter of 2009.

Results of Operations

Three Months Ended October 2, 2010 Compared to Three Months Ended October 3, 2009

The following table presents a summary of the operating information for the third quarters of 2010 and 2009:

(in thousands)	**2010**	*% of Revenue*	**2009**	*% of Revenue*	% Change
Revenues					
System sales	$ 133,439	*29 %*	$ 118,325	*29 %*	13 %
Support and maintenance	130,199	*28 %*	122,067	*30 %*	7 %
Services	191,090	*41 %*	162,122	*40 %*	18 %
Reimbursed travel	7,955	*2 %*	6,901	*2 %*	15 %
Total revenues	462,683	*100 %*	409,415	*100 %*	13 %
Costs of revenue					
Costs of revenue	79,148	*17 %*	69,479	*17 %*	14 %
Total margin	*383,535*	*83 %*	*339,936*	*83 %*	*13 %*
Operating expenses					
Sales and client service	189,320	*41 %*	171,415	*42 %*	10 %
Software development	67,257	*15 %*	66,752	*16 %*	1 %
General and administrative	32,966	*7 %*	31,059	*8 %*	6 %
Total operating expenses	289,543	*63 %*	269,226	*66 %*	8 %
Total costs and expenses	368,691	*80 %*	338,705	*83 %*	9 %
Operating earnings	93,992	*20.3 %*	70,710	*17.3 %*	33 %
Interest income (expense), net	87		180		
Other income (expense), net	5		(3)		
Income taxes	(33,212)		(22,493)		
Net earnings	$ 60,872		$ 48,394		26 %

Revenues & Backlog

Revenues increased 13% to $462.7 million for the third quarter 2010 from $409.4 million for the same period in 2009.

System sales, which include revenues from the sale of software, technology resale (hardware and sublicensed software), deployment period licensed software upgrade rights, installation fees, transaction processing and subscriptions, increased 13% to $133.4 million for the third quarter of 2010 from $118.3 million for the same period in 2009. The increase in system sales was driven by a strong increase in licensed software and technology resale.

Support and maintenance revenues increased 7% to $130.2 million during the third quarter of 2010 from $122.1 million during the same period in 2009. The increase is attributable to growth in *Cerner Millennium* applications for which support billing has been initiated.

Services revenue, which includes professional services excluding installation, and managed services, increased 18% to $191.1 million from $162.1 million for the same period in 2009. This increase is driven by growth in *CernerWorks*[SM] managed services as a result of continued demand for our hosting services and an increase in professional services due to increased implementation activities.

Contract backlog, which reflects new business bookings that have not yet been recognized as revenue, increased 24% in the third quarter of 2010 compared to the same period in 2009. This increase was driven by growth in new business bookings during the past four quarters, including continued strong levels of managed services bookings that typically have longer contract terms. A summary of our total backlog follows:

(In thousands)	October 2, 2010	October 3, 2009
Contract backlog	$ 4,018,475	$ 3,246,797
Support and maintenance backlog	642,436	604,389
Total backlog	$ 4,660,911	$ 3,851,186

Costs of Revenue

Cost of revenues remained flat at 17% of total revenues in the third quarter of 2010 and 2009. The cost of revenues includes the cost of reimbursed travel expense, third party consulting services and subscription content, computer hardware and sublicensed software purchased from hardware and software manufacturers for delivery to clients. It also includes the cost of hardware maintenance and sublicensed software support subcontracted to the manufacturers. Such costs, as a percent of revenues, typically have varied as the mix of revenue (software, hardware, maintenance, support, services and reimbursed travel) carrying different margin rates changes from period to period. Costs of revenues does not include the costs of our client service personnel who are responsible for delivering our service offerings, such costs are included in sales and client service expense.

Operating Expenses

Total operating expenses increased 8% to $289.5 million in the third quarter of 2010, compared with $269.2 million for the same period in 2009. Share-based compensation expense recognized impacted expenses as indicated below:

	Three Months Ended	
(In thousands)	2010	2009
Sales and client service expenses	$ 2,944	$ 2,315
Software development expense	1,861	1,132
General and administrative expenses	1,745	1,258
Total stock-based compensation expense	$ 6,550	$ 4,705

Sales and client service expenses as a percent of total revenues were 41% in the third quarter of 2010 as compared to 42% in the same period of 2009. These expenses increased 10% to $189.3 million in the third quarter of 2010, from $171.4 million in the same period of 2009. Sales and client service expenses include salaries of sales and client service personnel, depreciation and other expenses associated with our *CernerWorks* managed service business, communications expenses, unreimbursed travel expenses, expense for share-based payments, sales and marketing salaries and trade show and advertising costs. The increase was primarily attributable to growth in the managed services business and an increase in bad debt expense.

Software development expense increased 1% to $67.3 million for the third quarter of 2010 compared to $66.8 million for the same period in 2009. The small amount of the increase reflects our ongoing efforts to control spending growth relative to revenue growth. A summary of our total software development expense is as follows:

	Three Months Ended	
(In thousands)	2010	2009

Software development costs	$ 70,037	$ 69,940
Capitalized software costs	(20,199)	(19,878)
Capitalized costs related to share-based payments	(337)	(232)
Amortization of capitalized software costs	17,756	16,922
Total software development expense	$ 67,257	$ 66,752

General and administrative expenses as a percent of total revenues were 7%, in the third quarter of 2010, as compared to 8% for the same period in 2009. These expenses increased 6% to $33.0 million in the third quarter of 2010, from $31.1 million for the same period in 2009. General and administrative expenses include salaries for corporate, financial and administrative staffs, utilities, communications expenses, professional fees, transaction gains or losses on foreign currency and expense for share based payments. We recorded a net transaction loss on foreign currency of $0.9 million and a net transaction gain on foreign currency of $0.03 million in the third quarters of 2010 and 2009, respectively, which, along with a slight increase in other corporate expenses, accounted for the majority of the overall increase in general and administrative expenses.

Non-Operating Items

Net interest income was $0.09 million in the third quarter of 2010 compared to net interest income of $0.2 million in the third quarter of 2009. Interest income decreased to $1.8 million in the third quarter of 2010 from $2.4 million for the same period in 2009. Interest expense decreased to $1.7 million in the third quarter of 2010 from $2.2 million for the same period in 2009, due primarily to long-term debt payments made in the fourth quarter of 2009.

Other income was $0.01 million in the third quarter of 2010, compared to other expense of $0.03 million for the same period in 2009. Other income and expense in the third quarters 2010 and 2009 includes offsetting unrealized gains and losses included in earnings related to our auction rate securities and put-like settlement feature in the amounts of $1.2 million and $1.9 million, respectively. Refer to Liquidity and Capital Resources within this MD&A and Note 3 of the notes to condensed consolidated financial statements for additional information on our auction rate securities.

Our effective tax rate was 35% for the third quarter of 2010 and 32% for the third quarter of 2009. This increase is primarily due to the research and development tax credit not being extended for the 2010 tax year and a decrease in unrecognized tax benefits in the third quarter of 2009 as a result of the Internal Revenue Service completion of the 2007 income tax return and refund claim related to the foreign tax credit for the 2004, 2005 and 2006 income tax returns.

Operations by Segment

We have two operating segments, Domestic and Global. The Domestic segment includes revenue contributions and expenditures associated with business activity in the United States. The Global segment includes revenue contributions and expenditures linked to business activity in Aruba, Australia, Austria, Belgium, Canada, Cayman Islands, Chile, China (Hong Kong), Egypt, England, France, Germany, India, Ireland, Malaysia, Puerto Rico, Saudi Arabia, Singapore, Spain, Sweden, Switzerland and the United Arab Emirates.

The following table presents a summary of the operating information for the third quarters of 2010 and 2009:

(in thousands)		**2010**	*% of Revenue*		**2009**	*% of Revenue*	% Change
Domestic Segment							
Revenues	$	394,052	*100%*	$	338,508	*100%*	16%
Costs of revenue		64,150	*16%*		57,759	*17%*	11%
Operating expenses		102,605	*26%*		90,093	*27%*	14%
Total costs and expenses		166,755	*42%*		147,852	*44%*	13%
Domestic operating earnings		227,297	*58%*		190,656	*56%*	19%
Global Segment							
Revenues		68,631	*100%*		70,907	*100%*	-3%
Costs of revenue		14,998	*22%*		11,720	*17%*	28%
Operating expenses		29,482	*43%*		32,658	*46%*	-10%
Total costs and expenses		44,480	*65%*		44,378	*63%*	0%
Global operating earnings		24,151	*35%*		26,529	*37%*	-9%
Other, net		(157,456)			(146,475)		7%
Consolidated operating earnings	$	93,992		$	70,710		33%

Domestic Segment

Revenues increased 16% to $394.1 million in the third quarter of 2010 from $338.5 million in the same period in 2009. This increase was driven primarily by growth in licensed software, managed services and professional services.

Cost of revenues was 16% of revenues in the third quarter of 2010, compared to 17% of revenues in the same period in 2009. The decrease reflects the typically higher margins of licensed software, managed services and professional services.

Operating expenses increased 14% to $102.6 million in the third quarter of 2010, from $90.1 million in the same period in 2009, due primarily to growth in managed services and professional services expense.

Global Segment

Revenues decreased 3% to $68.6 million in the third quarter of 2010 from $70.9 million in the same period in 2009. This decrease was driven by decline in licensed software and professional services revenue, largely from our operations in France, partially offset by an increase in technology resale and support revenue.

Cost of revenues was 22% of revenues in the third quarter of 2010, compared with 17% in the same period of 2009. The higher cost of revenues in the third quarter of 2010 was driven by the increase in technology resale, which carries a higher cost of revenue.

Operating expenses decreased 10% to $29.5 million for the third quarter of 2010, from $32.7 million in the same period in 2009, primarily due to a decrease in personnel-related professional services expense, partially offset by an increase in bad debt expense.

Other, net

Operating results not attributed to an operating segment include expenses, such as software development, marketing, general and administrative, stock-based compensation and depreciation. These expenses increased 7% to $157.5 million in the third quarter of 2010 from $146.5 million in the same period in 2009. This increase was primarily due to growth in corporate personnel costs, somewhat offset by the previously discussed impact of foreign currency transaction gains and losses.

Nine Months Ended October 2, 2010 Compared to Nine Months Ended October 3, 2009
The following table presents a summary of the operating information for the first nine months of 2010 and 2009:

(in thousands)	**2010**	*% of Revenue*	**2009**	*% of Revenue*	% Change
Revenues					
System sales	$ 386,292	*29%*	$ 332,816	*28%*	16%
Support and maintenance	385,304	*29%*	370,210	*31%*	4%
Services	554,605	*41%*	479,251	*40%*	16%
Reimbursed travel	23,820	*2%*	23,266	*2%*	2%
Total revenues	1,350,021	*100%*	1,205,543	*100%*	12%
Costs of revenue					
Costs of revenue	225,443	*17%*	201,899	*17%*	12%
Total margin	*1,124,578*	*83%*	*1,003,644*	*83%*	*12%*
Operating expenses					
Sales and client service	566,943	*42%*	516,401	*43%*	10%
Software development	202,024	*15%*	196,578	*16%*	3%
General and administrative	99,611	*7%*	91,819	*8%*	8%
Total operating expenses	868,578	*64%*	804,798	*67%*	8%
Total costs and expenses	1,094,021	*81%*	1,006,697	*84%*	9%
Operating earnings	256,000	*19.0%*	198,846	*16.5%*	29%
Interest income (expense), net	2,291		(287)		
Other income (expense), net	(566)		414		
Income taxes	(91,090)		(66,004)		
Net earnings	$ 166,635		$ 132,969		25%

Revenues & Backlog

Revenues increased 12% to $1,350.0 million for the first nine months of 2010 from $1,205.5 million for the same period in 2009.

System sales, which include revenues from the sale of software, technology resale (hardware and sublicensed software), deployment period licensed software upgrade rights, installation fees, transaction processing and subscriptions, increased 16% to $386.3 million for the first nine months of 2010 from $332.8 million for the same period in 2009. The increase in system sales was driven by a strong increase in licensed software and technology resale.

Support and maintenance revenues increased 4% to $385.3 million during the first nine months of 2010 from $370.2 million during the same period in 2009. The increase is attributable to growth in *Cerner Millennium* applications for which support billing has been initiated.

Services revenue, which includes professional services excluding installation, and managed services, increased 16% to $554.6 million from $479.3 million for the same period in 2009. This increase is driven by growth in *CernerWorks* managed services as a result of continued demand for our hosting services and an increase in professional services due to increased implementation activities.

Contract backlog, which reflects new business bookings that have not yet been recognized as revenue, increased 24% in the first nine months of 2010 compared to the same period in 2009. This increase was driven by growth in new business bookings during the past four quarters, including continued strong levels of managed services bookings that typically have longer contract terms. A summary of our total backlog follows:

(In thousands)	October 2, 2010	October 3, 2009
Contract backlog	$ 4,018,475	$ 3,246,797
Support and maintenance backlog	642,436	604,389
Total backlog	$ 4,660,911	$ 3,851,186

Costs of Revenue

Cost of revenues remained flat at 17% of total revenues in the first nine months of 2010 and 2009. The cost of revenues includes the cost of reimbursed travel expense, third party consulting services and subscription content, computer hardware and sublicensed software purchased from hardware and software manufacturers for delivery to clients. It also includes the cost of hardware maintenance and sublicensed software support subcontracted to the manufacturers. Such costs, as a percent of revenues, typically have varied as the mix of revenue (software, hardware, maintenance, support, services and reimbursed travel) carrying different margin rates changes from period to period. Costs of revenues does not include the costs of our client service personnel who are responsible for delivering our service offerings, such costs are included in sales and client service expense.

Operating Expenses

Total operating expenses increased 8% to $868.6 million in the first nine months of 2010, compared with $804.8 million for the same period in 2009. Share-based compensation expense recognized impacted expenses as indicated below:

	Nine Months Ended	
(In thousands)	2010	2009
Sales and client service expenses	$ 7,723	$ 5,401
Software development expense	4,903	3,134
General and administrative expenses	5,277	3,676
Total stock-based compensation expense	$ 17,903	$ 12,211

Sales and client service expenses as a percent of total revenues were 42% in the first nine months of 2010 as compared to 43% in the same period of 2009. These expenses increased 10% to $566.9 million in the first nine months of 2010, from $516.4 million in the same period of 2009. Sales and client service expenses include salaries of sales and client service personnel, depreciation and other expenses associated with our *CernerWorks* managed service business, communications expenses, unreimbursed travel expenses, expense for share-based payments, sales and marketing salaries and trade show and advertising costs. The increase was primarily attributable to growth in the managed services business, a higher level of professional services expenses and an increase in bad debt expense.

Software development expense increased 3% to $202.0 million for the first nine months of 2010 compared to $196.6 million for the same period in 2009. The increase in software development costs is related to increased development activity on *Cerner Millennium* and related solutions. The small amount of increase reflects our ongoing efforts to control spending growth relative to revenue growth. A summary of our total software development expense is as follows:

	Nine Months Ended	
(In thousands)	2010	2009
Software development costs	$ 213,793	$ 209,476
Capitalized software costs	(60,802)	(58,081)
Capitalized costs related to share-based payments	(982)	(618)
Amortization of capitalized software costs	50,015	45,801
Total software development expense	$ 202,024	$ 196,578

General and administrative expenses as a percent of total revenues were 7%, in the third quarter of 2010, as compared to 8% for the same period in 2009. These expenses increased 8% to $99.6 million in the first nine months of 2010, from $91.8 million for the same period in 2009. General and administrative expenses include salaries for corporate, financial and administrative staffs, utilities, communications expenses, professional fees, transaction gains or losses on foreign currency and expense for share based payments. We recorded a net transaction loss on foreign currency of $0.3 million and a gain of $4.0 million in the first nine months of 2010 and 2009, respectively, which along with an increase in corporate personnel costs, accounted for the majority of the overall increase in general and administrative expenses.

Non-Operating Items

Net interest income was $2.3 million in the first nine months of 2010 compared to net interest expense of $0.3 million in the first nine months of 2009. Interest income increased to $7.6 million in the first nine months of 2010 from $6.0 million for the same period in 2009, due primarily to growth in investments and an increase in investment returns. Interest expense decreased to $5.3 million in the first nine months of 2010 from $6.3 million for the same period in 2009, due primarily to long-term debt payments made in the fourth quarter of 2009.

Other expense was $0.6 million in the first nine months of 2010, compared to other income of $0.4 million for the same period in 2009. Other income and expense in the first nine months of 2010 and 2009 includes offsetting unrealized gains and losses included in earnings related to our auction rate securities and put-like settlement feature in the amounts of $6.9 million and $11.8 million, respectively. Refer to Liquidity and Capital Resources within this MD&A and Note 3 of the notes to condensed consolidated financial statements for additional information on our auction rate securities.

Our effective tax rate was 35% for the first nine months of 2010 and 33% for the first nine months of 2009. This increase is primarily due to the research and development tax credit not being extended for the 2010 tax year and a decrease in unrecognized tax benefits in the third quarter of 2009 as a result of the Internal Revenue Service completion of the 2007 income tax return and refund claim related to the foreign tax credit for the 2004, 2005 and 2006 income tax returns.

Operations by Segment

We have two operating segments, Domestic and Global. The Domestic segment includes revenue contributions and expenditures associated with business activity in the United States. The Global segment includes revenue contributions and expenditures linked to business activity in Aruba, Australia, Austria, Belgium, Canada, Cayman Islands, Chile, China (Hong Kong), Egypt, England, France, Germany, India, Ireland, Malaysia, Puerto Rico, Saudi Arabia, Singapore, Spain, Sweden, Switzerland and the United Arab Emirates.

The following table presents a summary of the operating information for the first nine months of 2010 and 2009:

(in thousands)	**2010**	*% of Revenue*	**2009**	*% of Revenue*	% Change
Domestic Segment					
Revenues	$ 1,130,384	*100%*	$ 997,441	*100%*	13%
Costs of revenue	189,540	*17%*	169,567	*17%*	12%
Operating expenses	311,663	*28%*	272,552	*27%*	14%
Total costs and expenses	501,203	*44%*	442,119	*44%*	13%
Domestic operating earnings	629,181	*56%*	555,322	*56%*	13%
Global Segment					
Revenues	219,637	*100%*	208,102	*100%*	6%
Costs of revenue	35,903	*16%*	32,333	*16%*	11%
Operating expenses	93,577	*43%*	97,179	*47%*	-4%

Total costs and expenses	129,480	*59%*	129,512	*62%*	0%
Global operating earnings	90,157	*41%*	78,590	*38%*	15%
Other, net	(463,338)		(435,067)		6%
Consolidated operating earnings	$ 256,000		$ 198,846		29%

Domestic Segment

Revenues increased 13% to $1,130.4 million in the first nine months of 2010 from $997.4 million the same period in 2009. This increase was driven by growth in licensed software, managed services and professional services.

Cost of revenues remained flat at 17% of revenues in the first nine months of 2010, compared to the same period in 2009.

Operating expenses increased 14% to $311.7 million in the first nine months of 2010, from $272.6 million in the same period in 2009, due primarily to growth in managed services expense, professional services expense and bad debt expense.

Global Segment

Revenues increased 6% to $219.6 million in the first nine months of 2010 from $208.1 million in the same period in 2009. This increase was driven by a change in estimates for certain contracts that rely on estimates as part of contract accounting and improved licensed software and support revenue, mostly from United Kingdom and the Middle East region, slightly offset by a decline from France.

Cost of revenues remained flat at 16% of revenues in the first nine months of 2010, compared to the same period in 2009.

Operating expenses decreased 4% to $93.6 million for the first nine months of 2010, from $97.2 million in the same period in 2009, primarily due to a decrease in personnel-related professional services expense, partially offset by an increase in bad debt expense.

Other, net

Operating results not attributed to an operating segment include expenses, such as software development, marketing, general and administrative, stock-based compensation and depreciation. These expenses increased 6% to $463.3 million in the first nine months of 2010 from $435.1 million in the same period in 2009. This increase was primarily due to growth in corporate personnel costs and by the previously discussed impact of foreign currency transaction gains and losses.

Liquidity and Capital Resources

Our liquidity is influenced by many factors, including the amount and timing of our revenues, our cash collections from our clients and the amounts we invest in software development, acquisitions and capital expenditures.

Our principal sources of liquidity are our cash, cash equivalents, which consist of money market funds, time deposits, and bonds with original maturities of less than 90 days, and short-term investments. At October 2, 2010, we had cash of $183.8 million, cash equivalents of $28.0 million and short-term investments of $353.5 million compared to cash of $144.8 million, cash equivalents of $97.0 million and short-term investments of $317.1 million at January 2, 2010.

Additionally, we maintain a $90 million, multi-year revolving credit facility, which provides an unsecured revolving line of credit for working capital purposes. Interest is payable at a rate based on prime or LIBOR plus a spread that varies depending on the net worth ratios maintained. The agreement contains certain net worth, current ratio and fixed charge coverage covenants and provides certain restrictions on our ability to borrow, incur liens, sell assets and pay dividends. The current agreement expires on May 31, 2013. As of October 2, 2010, we had no outstanding borrowings under this agreement and we are not aware of any violations of the covenants.

We believe that our present cash position, together with cash generated from operations, short-term investments and, if necessary, our available lines of credit, will be sufficient to meet anticipated cash requirements during 2010.

During the second quarter of 2008, Fujitsu Services Limited s (Fujitsu) contract as the prime contractor in the National Health Service (NHS) initiative to automate clinical processes and digitize medical records in the Southern region of England was terminated by the NHS. This had the effect of automatically terminating our subcontract for the project. We are in dispute with Fujitsu regarding Fujitsu s obligation to pay the amounts comprised of accounts receivable and contracts receivable related to that subcontract, and we are working with Fujitsu to resolve these issues based on processes provided for in the contract. Part of that process requires resolution of disputes between Fujitsu and the NHS regarding the contract termination. As of October 2, 2010, it remains unlikely that the matter will be resolved in the next 12 months. Therefore these receivables have been classified as long-term and represent the significant majority of other long-term assets as of the third quarter ended October 2, 2010. While the ultimate collectability of the receivables pursuant to this process is uncertain, we believe that we have valid and equitable grounds for recovery of such amounts and that collection of recorded amounts is probable.

In February and March 2008, liquidity issues in the global credit markets resulted in the progressive failure of auctions representing all the auction rate securities held by us. During the fourth quarter of 2008, we entered into a settlement

agreement with the investment firm that sold us the auction rate securities. Under the terms of the settlement agreement, we received the right to redeem the securities at par value during a period from mid-2010 through mid-2012. The settlement is in effect a put-like instrument with a fair value generally equal to the difference between the auction rate securities fair value and par value. In the fourth quarter of 2009, these securities were reclassified to short term investments based on our intention to exercise the put-like settlement feature and redeem the securities within the next year. At October 2, 2010, we held auction rate securities with a par value of $21.3 million and an estimated fair value of $18.5 million.

We anticipate that any future changes in the fair value of the put-like feature will be offset by the changes in the fair value of the related auction rate securities with no material net impact to the Condensed Consolidated Statements of Operations. We do not expect the auction failures to impact our ability to fund our working capital needs, capital expenditures or other business requirements.

The following table summarizes our cash flows in the first nine months of 2010 and 2009:

	Nine Months Ended	
(In thousands)	2010	2009
Cash flows from operating activities	$ 334,697	$ 239,158
Cash flows from investing activities	(407,843)	(174,733)
Cash flows from financing activities	40,262	33,043
Effect of exchange rate changes on cash	2,908	10
Total change in cash and cash equivalents	$ (29,976)	$ 97,478
Free cash flow (non-GAAP)	$ 197,573	$ 90,597

<u>*Cash from Operating Activities*</u>

Cash flow from operations increased in the first nine months of 2010 as compared to the same period of 2009 due primarily to the increase in cash impacting earnings and cash provided by working capital. During the first nine months of 2010 and 2009, we received total client cash collections of $1,402.6 million and $1,304.3 million, respectively, of which 3% and 4%, respectively, were received from third party client financing arrangements and non-recourse payment assignments. Days sales outstanding was 91 days for the third quarter of 2010 compared to 88 days in the second quarter of 2010 and 105 days in the third quarter of 2009. The majority of this year-over-year decline is driven by the reclassification of our Fujitsu receivable to other long-term assets during the fourth quarter of 2009, which is not included in our days sales outstanding calculation. Revenues provided under support and maintenance agreements represent recurring cash flows. Support and maintenance revenues increased 4% in the first nine months of 2010 compared to the first nine months of 2009. We expect these revenues to continue to grow as the base of installed *Cerner Millennium* systems grows.

<u>*Cash from Investing Activities*</u>

	Nine Months Ended	
(In thousands)	2010	2009
Capital purchases	$ (75,341)	$ (89,863)
Capitalized software development costs	(61,783)	(58,698)
Purchases of investments, net of maturities	(248,199)	(13,727)
Acquisition of businesses, net of cash acquired	(14,486)	(3,529)

Other, net		(8,034)		(8,916)
Total cash flows from investing activities	$	(407,843)	$	(174,733)

Cash flows from investing activities consist primarily of capital spending and our short-term investment activities. Capital spending consists of capitalized equipment purchases primarily to support growth in our *CernerWorks* managed services business, capitalized land, building and improvement purchases to support our facilities requirements and capitalized spending to support our ongoing software development initiatives. Capital spending in 2010 is expected to approximate our 2009 levels.

In addition, during the first quarter 2010, we completed our acquisition of IMC Health Care, Inc. for approximately $14.5 million, net of the cash acquired.

Cash from Financing Activities

(In thousands)	Nine Months Ended 2010	2009
Long-term debt repayments	$ (2,404)	$ (7,065)
Cash from option exercises (including excess tax benefits)	41,150	38,220
Other, net	1,516	1,888
Total cash flows from financing activities	$ 40,262	$ 33,043

Our primary financing obligations are long-term debt repayments. In the fourth quarter of 2009, we commenced payment on the first of seven equal annual installments on our 5.54% Great Britain Pound denominated Note Agreement as well as on the first of four equal annual installments on our 6.42% Series B Senior Notes. Based on debts currently outstanding and current exchange rates, we expect our debt repayments to approximate $25 million per year through 2012 and approximately $15 million per year from 2013 through 2016.

Free Cash Flow

(In thousands)	Three Months Ended 2010	2009	Nine Months Ended 2010	2009
Cash flows from operating activities	$ 118,956	$ 73,402	$ 334,697	$ 239,158
Capital purchases	(19,330)	(24,140)	(75,341)	(89,863)
Capitalized software development costs	(20,535)	(20,110)	(61,783)	(58,698)
Free cash flow (non-GAAP)	$ 79,091	$ 29,152	$ 197,573	$ 90,597

Free Cash Flow increased $50 million in the third quarter of 2010 and increased $107 million in the first nine months of 2010, as compared to the same respective periods in 2009, which we believe reflects continued strengthening of our earnings quality. Free Cash Flow is a non-GAAP financial measure used by management along with GAAP results to analyze its earnings quality and overall cash generation of the business. The presentation of Free Cash Flow is not meant to be considered in isolation, as a substitute for, or superior to, GAAP results and investors should be aware that non-GAAP measures have inherent limitations and should be read only in conjunction with our consolidated financial statements prepared in accordance with GAAP. Free Cash Flow may also be different from similar non-GAAP financial measures used by other companies and may not be comparable to similarly titled captions of other companies due to potential inconsistencies in the method of calculation. We believe Free Cash Flow is important to enable investors to better understand and evaluate our ongoing operating results and allows for greater transparency in the review of our overall financial, operational and economic performance.

Recent Accounting Pronouncements

In July 2010, Accounting Standards Update (ASU) 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, was issued and amends ASC 310, *Receivables*. ASU 2010-20 requires increased disclosures about the credit quality of financing receivables and allowances for credit losses, including disclosure about credit quality indicators, past due information and modifications of financing receivables. Trade accounts receivable with maturities of one year or less are excluded from the disclosure requirements. The guidance is generally effective for reporting periods ending after December 15, 2010. We are currently evaluating the impact the adoption of ASU 2010-20 will have on our consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

No material changes.

Item 4. Controls and Procedures

a) Evaluation of disclosure controls and procedures. The Company s Chief Executive Officer (CEO) and Chief Financial Officer (CFO) have evaluated the effectiveness of the Company s disclosure controls and procedures (as defined in the Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by the Quarterly Report (the Evaluation Date). They have concluded that, as of the Evaluation Date, these disclosure controls and procedures were effective to ensure that material information relating to the Company and its consolidated subsidiaries would be made known to them by others within those entities and would be disclosed on a timely basis. The CEO and CFO have concluded that the Company s disclosure controls and procedures are designed, and are effective, to give reasonable assurance that the information required to be disclosed by the Company in reports that it files under the Exchange Act is recorded, processed, summarized and reported within the time period specified in the rules and forms of the SEC. They have also concluded that the Company s disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports that are filed or submitted under the Exchange Act are accumulated and communicated to the Company s management, including the CEO and CFO, to allow timely decisions regarding required disclosure.

b) There were no changes in the Company s internal controls over financial reporting during the three months ended October 2, 2010 that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting.

c) The Company s management, including its CEO and CFO, has concluded that our disclosure controls and procedures and internal control over financial reporting are designed to provide reasonable assurance of achieving their objectives and are effective at that reasonable assurance level. However, the Company s management can provide no assurance that our disclosure controls and procedures or our internal control over financial reporting can prevent all errors and all fraud under all circumstances. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been or will be detected. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Part II. Other Information

Item 6. Exhibits

(a) Exhibits

10(a)	Cerner Corporation 2005 Enhanced Severance Pay Plan as Amended and Restated August 15, 2010.
31.1	Certification of Neal L. Patterson, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Marc G. Naughton, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

SIGNATURES

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

CERNER CORPORATION
Registrant

October 29, 2010
Date

By: /s/Marc G. Naughton
Marc G. Naughton
Chief Financial Officer
(duly authorized officer and principal financial officer)