INTERNATIONAL GAME TECHNOLOGY
Form 10-Q
May 11, 2011

United States
Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended April 2, 2011

OR

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

For the transition period from ____ to ____

Commission File Number 001-10684

International Game Technology

Nevada	88-0173041
(State or other jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

9295 Prototype Drive, Reno, Nevada 89521
(Address of Principal Executive Offices)(Zip Code)

Registrant's Telephone Number, Including Area code: (775) 448-7777

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 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 [ ]	Smaller reporting company [ ]

(Do not check if a 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]

The number of shares outstanding of each of the registrant's classes of common stock, as of May 6, 2011:
299.9 million shares of common stock at $.00015625 par value.

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GLOSSARY OF TERMS AND ABBREVIATIONS (as used in this document)

Fiscal dates--as presented:	Fiscal dates--actual:
March 31, 2011	April 2, 2011
March 31, 2010	April 3, 2010
September 30, 2010	October 2, 2010

Abbreviation/term	Definition
Anchor	Anchor Gaming
ARS	auction rate securities
ASU	Accounting Standards Update
5.5% Bonds	5.5% fixed rate notes due 2020
7.5% Bonds	7.5% fixed rate notes due 2019
bps	basis points
CCSC	Colorado Central Station Casino
CEO	chief executive officer
CFO	chief financial officer
CLS	China LotSynergy Holdings, Ltd.
DCF	discounted cash flow
DigiDeal	DigiDeal Corporation
EBITDA	earnings before interest, taxes, depreciation, and amortization
EPA	Environmental Protection Agency
EPS	earnings per share
ERISA	Employee Retirement Income Security Act
FASB	Financial Accounting Standards Board
GAAP	generally accepted accounting principles
IGT, we, our, the Company	International Game Technology and its consolidated entities
IP	intellectual property
IRS	Internal Revenue Service
LIBOR	London inter-bank offering rate
MDA	management’s discussion and analysis of financial condition and results of operations
Notes	3.25% convertible notes due 2014
OSHA	Occupational Safety & Health Administration
pp	percentage points
R&D	research and development
sbX™	IGT’s complete server-based player experience management solution
SEC	Securities and Exchange Commission
SIP	2002 Stock Incentive Plan
UK	United Kingdom
US	United States
UTBs	unrecognized tax benefits
VIE	variable interest entity
WAP	wide area progressive
*	not meaningful (in tables)

PART I – FINANCIAL INFORMATION

Item 1. Unaudited Consolidated Interim Financial Statements

CONSOLIDATED INCOME STATEMENTS

(In millions, except per share amounts)	Quarters Ended March 31, 2011	Quarters Ended March 31, 2010	Six Months Ended March 31, 2011	Six Months Ended March 31, 2010
Revenues				
Gaming operations	$277.6	$280.1	$538.3	$556.8
Product sales	214.7	206.7	418.8	445.1
Total revenues	492.3	486.8	957.1	1,001.9
Costs and operating expenses				
Cost of gaming operations	104.7	107.0	200.6	211.0
Cost of product sales	95.6	107.9	188.3	223.2
Selling, general and administrative	92.9	84.7	177.8	172.0
Research and development	51.3	51.1	103.0	96.5
Depreciation and amortization	16.9	18.7	35.1	38.1
Impairment	-	53.1	-	53.1
Total costs and operating expenses	361.4	422.5	704.8	793.9
Operating income	130.9	64.3	252.3	208.0
Other income (expense)				
Interest income	13.3	15.4	26.6	31.4
Interest expense	(35.6)	(39.0)	(71.0)	(82.2)
Other	(1.0)	0.6	3.2	(0.7)
Total other income (expense)	(23.3)	(23.0)	(41.2)	(51.5)
Income from continuing operations before tax	107.6	41.3	211.1	156.5
Income tax provision	38.0	15.6	68.1	55.4
Income from continuing operations	69.6	25.7	143.0	101.1
Income (loss) from discontinued operations, net of tax	-	(25.0)	0.3	(27.1)
Net income	$69.6	$0.7	$143.3	$74.0
Basic earnings (loss) per share				
Continuing operations	$0.23	$0.08	$0.48	$0.34
Discontinued operations	-	(0.08)	-	(0.09)
Net income	$0.23	$-	$0.48	$0.25
Diluted earnings (loss) per share				
Continuing operations	$0.23	$0.08	$0.48	$0.34
Discontinued operations	-	(0.08)	-	(0.09)
Net income	$0.23	$-	$0.48	$0.25
Cash dividends declared per share	$0.06	$0.06	$0.12	$0.12
Weighted average shares outstanding				
Basic	298.4	295.9	298.0	295.5
Diluted	299.9	297.3	299.4	297.7

See accompanying notes

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CONSOLIDATED BALANCE SHEETS

(In millions, except par value)	March 31, 2011	September 30, 2010
Assets		
Current assets		
Cash and equivalents	$305.9	$158.4
Restricted cash and investment securities	65.4	88.1
Restricted cash and investment securities of VIEs	2.1	2.4
Jackpot annuity investments	49.4	49.5
Jackpot annuity investments of VIEs	15.3	15.6
Accounts receivable, net	318.3	290.3
Current maturities of contracts and notes receivable, net	177.1	184.1
Inventories	106.7	97.6
Deferred income taxes	87.8	84.3
Other assets and deferred costs	157.4	232.1
Total current assets	1,285.4	1,202.4
Property, plant and equipment, net	585.0	586.7
Jackpot annuity investments	287.0	299.1
Jackpot annuity investments of VIEs	59.2	61.7
Contracts and notes receivable, net	133.2	171.9
Goodwill	1,153.0	1,151.6
Other intangible assets, net	179.6	202.1
Deferred income taxes	129.8	136.8
Other assets and deferred costs	170.2	194.7
Total Assets	$3,982.4	$4,007.0
Liabilities and Shareholders' Equity		
Liabilities		
Current liabilities		
Accounts payable	$78.3	$84.6
Jackpot liabilities, current portion	152.0	179.1
Accrued employee benefits	17.2	23.9
Accrued income taxes	3.3	1.8
Dividends payable	18.0	17.9
Other accrued liabilities	257.8	275.0
Total current liabilities	526.6	582.3
Long-term debt	1,549.1	1,674.3
Jackpot liabilities	374.0	391.8
Other liabilities	148.5	124.3
Total Liabilities	2,598.2	2,772.7
Commitments and Contingencies		
Shareholders' Equity		
Common stock: $.00015625 par value; 1,280.0 shares authorized; 340.6 and 339.1 issued; 299.4 and 298.1 outstanding	0.1	0.1
Additional paid-in capital	1,508.4	1,473.7
Treasury stock at cost: 41.2 and 41.0 shares	(804.2)	(802.0)
Retained earnings	659.2	551.8
Accumulated other comprehensive income	20.7	10.7

Total Equity	1,384.2	1,234.3
Total Liabilities and Shareholders' Equity	$3,982.4	$4,007.0

See accompanying notes

CONSOLIDATED STATEMENTS OF CASH FLOWS

Six Months Ended March 31, (In millions)	2011	2010
Operating		
Net income	$ 143.3	$ 74.0
Adjustments:		
Depreciation and amortization	109.2	120.2
Discounts and deferred issuance costs	22.4	24.3
Share-based compensation	22.9	20.6
Impairment	-	59.8
Excess tax benefits from employee stock plans	(2.8)	(6.9)
(Gain) loss on assets sold	(11.9)	(1.2)
Other, net	6.2	15.1
Changes in operating assets and liabilities, excluding acquisitions:		
Receivables	3.8	25.4
Inventories	(6.2)	31.9
Other assets and deferred costs	18.1	39.4
Income taxes, net of employee stock plans	50.5	(16.3)
Accounts payable and accrued liabilities	(35.4)	(75.2)
Jackpot liabilities	(56.4)	(34.4)
Net operating cash flows	263.7	276.7
Investing		
Capital expenditures	(89.3)	(116.8)
Proceeds from assets sold	9.2	5.0
Investment securities, net	-	13.1
Jackpot annuity investments, net	26.6	29.3
Changes in restricted cash	23.0	0.2
Loans receivable cash advanced	(0.5)	(17.7)
Loans receivable payments received	14.8	3.3
Unconsolidated affiliates, net	16.5	(4.9)
Business/VIE acquisition/deconsolidation	-	(1.4)
Net investing cash flows	0.3	(89.9)
Financing		
Debt proceeds	95.0	1,016.5
Debt repayments	(195.0)	(1,158.4)
Debt issuance costs	-	(0.1)
Employee stock plan proceeds	13.9	13.3
Excess tax benefits from employee stock plans	2.8	6.9
Dividends paid	(35.8)	(35.6)
Net financing cash flows	(119.1)	(157.4)
Foreign exchange rates effect on cash and equivalents	2.6	(4.3)
Net change in cash and equivalents	147.5	25.1
Beginning cash and equivalents	158.4	146.7
Ending cash and equivalents	$ 305.9	$ 171.8

See accompanying notes

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SUPPLEMENTAL CASH FLOWS INFORMATION

“Depreciation and amortization” reflected in the cash flows statements are comprised of amounts presented separately on the income statements, plus “depreciation and amortization” included in cost of gaming operations, cost of product sales and discontinued operations.

Six Months Ended March 31, (In millions)	2011	2010
Unconsolidated affiliates		
Investment in	$ -	$ (4.9)
Sales proceeds	16.5	-
Net	$ 16.5	$ (4.9)
Jackpot funding		
Change in jackpot liabilities	$ (56.4)	$ (34.4)
Jackpot annuity purchases	(3.8)	(2.6)
Jackpot annuity proceeds	30.4	31.9
Net change in jackpot annuity investments	26.6	29.3
Net jackpot funding	$ (29.8)	$ (5.1)
Capital expenditures		
Property, plant and equipment	$ (8.4)	$ (16.4)
Gaming operations equipment	(80.2)	(98.3)
Intellectual property	(0.7)	(2.1)
Total	$ (89.3)	$ (116.8)
Payments		
Interest	$ 37.6	$ 47.8
Income taxes	15.7	68.6
Non-cash investing and financing items:		
Accrued capital asset additions	$ 0.2	$ 1.8
Interest accretion for jackpot annuity investments	11.5	12.7
Business acquisitions/purchase price adjustments and VIE deconsolidations		
Fair value of assets	$ -	$ (0.8)
Fair value of liabilities	-	(2.2)

See accompanying notes

NOTES TO UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION AND CONSOLIDATION

Our fiscal year is reported on a 52/53-week period ending on the Saturday nearest to September 30 each year. Similarly, our quarters end on the Saturday nearest to the last day of the quarter end month. For simplicity, fiscal periods in this report were presented using the calendar month end as outlined in the table below.

	Period End	
	Actual	Presented as
Current quarter	April 2, 2011	March 31, 2011
Prior year quarter	April 3, 2010	March 31, 2010
Prior fiscal year end	October 2, 2010	September 30, 2010

Our consolidated interim financial statements include the accounts of International Game Technology (IGT, we, our, or the Company), including all majority-owned or controlled subsidiaries and VIEs for which we are the primary beneficiary. All appropriate inter-company accounts and transactions have been eliminated.

Our consolidated interim financial statements for the current quarter ended March 31, 2011 have been prepared without audit and certain information and footnote disclosures have been condensed or omitted in conformity with SEC and US GAAP requirements on a basis consistent with the corresponding quarter ended March 31, 2010, and as appropriate, with the audited financial statements for the fiscal year ended September 30, 2010.

Our consolidated interim financial statements include all adjustments of a normal recurring nature necessary to fairly state our consolidated results of operations, financial position, and cash flows for all periods presented. Interim period results are not necessarily indicative of full year results. This quarterly report on Form 10-Q should be read in conjunction with our Annual Report on Form 10-K for the year ended September 30, 2010.

Use of Estimates

Our consolidated interim financial statements are prepared in conformity with US GAAP. Accordingly, we are required to make estimates, judgments and assumptions that we believe are reasonable based on our historical experience, contract terms, observance of known trends in our company and the industry as a whole, and information available from other outside sources. Our estimates affect reported amounts for assets, liabilities, revenues, expenses, and related disclosures. Actual results may differ from initial estimates.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Receivables

Allowances for Credit Losses

We maintain allowances for credit losses related to accounts receivable and customer financing where collectability is uncertain. We evaluate the adequacy of our allowances for credit losses on a quarterly basis and consider a number of factors applicable to all of our customer receivables and financing, including customers' financial condition, historical customer collection experience, receivable aging, economic conditions, legal environment, and regulatory landscape.

Customer Financing

Our customer financing portfolio is comprised of two classes, contracts and notes. Our contracts include extended payment terms granted to qualifying customers for periods from one to five years and are secured by the related products sold. Our notes consist of development financing loans granted to select customers to assist in the funding of new or expanding gaming facilities, generally under terms of one to seven years and are secured by the developed property and/or other assets. Interest income on contracts and notes is recognized at prevailing market rates.

We place an internally assigned risk grade on each contract and note in our customer financing portfolio. Internally assigned risk grades fall into three categories (low, medium, high), based on a number of factors, including customer size, type, financial condition, historical collection experience, account aging, and credit ratings derived from credit reporting agencies and other industry trade reports. The high risk category includes most of our development financing loans in new markets and customers in regions with a history of currency or economic instability, such as South/Central America. Many of our high risk loans are performing according to contract and do not warrant an allowance. Internally assigned risk grades on each contract and note are evaluated on a quarterly basis.

Customer financing is classified as past due when a scheduled payment is not received within 30 days of a payment notice. Initially customer financing with past due payments are collectively evaluated for impairment. Contracts and notes are evaluated individually for impairment (specific reserves) when collectability becomes uncertain due to events and circumstances, such as bankruptcy and tax or legal issues, that cause an adverse change in a customer's cash flows or financial condition. Accounts placed on specific reserve are simultaneously evaluated for probability of collection, which is used to determine the amount of the specific reserve. All changes in the net carrying amount of our contracts and notes are recorded as adjustments to bad debt expense or impairment.

When collection is deemed unlikely (typically reserved at 50% or greater) during our quarterly review as discussed above, the contract or note is placed on nonaccrual status and interest income is recognized on a cash basis. Uncollectible contracts or notes are written off when all reasonable collection efforts have been exhausted and it is determined that there is minimal chance of any kind of recovery, such as a customer property closure, bankruptcy restructuring or finalization, or other conditions that severely impact a customer's ability to repay amounts owed.

Recently Adopted Accounting Standards or Updates

Credit Quality of Financing Receivables and Allowances for Credit Losses

At the beginning of fiscal 2011, we adopted accounting standards issued in July 2010 to address the FASB concerns about the sufficiency, transparency, and robustness of credit risk disclosures for financing receivables and the related allowances for credit losses. The required information is designed to enable a better understanding of:

- the nature of credit risk inherent in our portfolio of financing receivables
- how credit risk is analyzed to determine the allowances for credit losses
- changes in and reasons for changes in the allowances for credit losses

These ASU disclosures were effective for our first quarter of fiscal 2011, except for allowance roll-forward disclosures effective with our second quarter of fiscal 2011 and troubled debt restructuring disclosures effective with reporting for our fiscal year ending September 30, 2011. The adoption of this ASU did not and will not have a material impact on our results of operations, financial position, or cash flow. See Note 2 above and Note 7.

Consolidation of Variable Interest Entities

At the beginning of fiscal 2011, we adopted accounting standards issued in June 2009, which require reassessment of our primary beneficiary position in VIE arrangements on an on-going basis and adds further disclosures about our involvement in VIEs. The revised standard also replaces the quantitative-based risks and rewards approach with a qualitative approach focused on determining which enterprise has the power to direct VIE activities that most significantly impact its economic performance and is obligated to absorb losses or has the rights to receive the most significant benefit from the VIE. The adoption of this ASU did not have a material impact on our results of operations, financial position, or cash flows.

Recently Issued Accounting Standards or Updates—Not Yet Adopted

Fair Value Measurement Disclosures

In January 2010, the FASB issued an ASU which will require supplemental disclosures related to purchases, sales, issuances, and settlements of fair value instruments within the Level 3 reconciliation. This ASU will be effective for our first quarter of fiscal 2012 and is not expected to have a material impact on our financial statements.

Accruals for Casino Jackpot Liabilities

In April 2010, the FASB issued an ASU clarifying that jackpot liabilities should not be accrued before they are won if the payout can be avoided. The ASU will be applied prospectively with a cumulative-effect adjustment in retained earnings at the beginning of our first quarter of fiscal 2012. We continue to evaluate the extent to which this guidance will impact our results of operations, financial position, or cash flows.

Troubled Debt Restructuring

In April 2011, the FASB issued an ASU to modify the way creditors identify and disclose troubled debt restructurings. The ASU will be effective for our fiscal year ending September 30, 2011 and must be applied retrospectively to the beginning of fiscal 2011. This ASU is not expected to have a material impact on our financial statements.

3. VARIABLE INTEREST ENTITIES AND AFFILIATES

Variable Interest Entities

New Jersey regulation requires that annuitized WAP jackpot payments to winners be administered through an individual trust set up for each WAP system. These trusts are VIEs. We determined that IGT was the primary consolidating beneficiary, because these VIE trusts are designed for the sole purpose of administering jackpot payments for IGT WAP winners and IGT guarantees all liabilities of the trusts. The assets of these consolidated VIEs can only be used to settle trust obligations and have been segregated on our balance sheet.

The consolidation of these VIEs primarily increases jackpot liabilities and related assets, as well as interest income and equivalent offsetting interest expense. Consolidated VIE trust assets and equivalent liabilities totaled $76.6 million at March 31, 2011 and $79.7 million at September 30, 2010.

Investments in Unconsolidated Affiliates

China LotSynergy Holdings, Ltd.

During the first quarter of fiscal 2011, we sold our CLS stock investment for net proceeds of $16.5 million and recognized a gain of $4.3 million.

At March 31, 2011, the fair value of our CLS convertible note and default put derivative together totaled $21.4 million. The adjusted cost basis of the note, including the conversion option, totaled $19.8 million. We determined that the conversion option did not qualify as a freestanding derivative requiring bifurcation at March 31, 2011. See Note 15 and Note 16 for additional information about CLS derivatives and fair value assumptions.

4. INVENTORIES

(In millions)	March 31, 2011	September 30, 2010
Raw materials	$ 61.2	$ 54.5
Work-in-process	4.1	3.9
Finished goods	41.4	39.2
Total	$ 106.7	$ 97.6

5. PROPERTY, PLANT AND EQUIPMENT

(In millions)	March 31, 2011	September 30, 2010
Land	$ 62.7	$ 62.7
Buildings	231.0	230.9
Leasehold improvements	15.9	14.6
Machinery, furniture and equipment	293.3	286.0
Gaming operations equipment	810.1	804.9
Total	1,413.0	1,399.1
Less accumulated depreciation	(828.0)	(812.4)
Property, plant and equipment, net	$ 585.0	$ 586.7

6. SHARE-BASED COMPENSATION

The amount, frequency, and terms of share-based awards may vary based on competitive practices, operating results, and government regulations. SIP grants generally vest over three to five years, either in ratable annual increments or 100% at the end of the vesting period. New shares of IGT common stock are issued upon exercises of stock options, vesting of restricted share units, or restricted share grants. Our current practice is generally to grant restricted share awards in the form of units without dividends. Forfeitures occur primarily when employment is terminated prior to vesting.

At March 31, 2011, 25.5 million shares were available for grant under the IGT SIP. Each restricted share or unit counts as two shares against this allowance beginning January 11, 2011. Unrecognized costs related to share-based awards outstanding at March 31, 2011 totaled $95.9 million and are expected to be recognized over a weighted average period of 1.9 years.

SIP Activity As Of And For The Six Months Ended March 31, 2011

Options	Shares (thousands)	Weighted Average Exercise Price (per share)	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (millions)
Outstanding at beginning of fiscal year	16,843	$ 21.38		
Granted	4,671	15.71		
Exercised	(573)	11.37		
Forfeited				