

PITNEY BOWES INC /DE/  
Form 10-Q  
November 02, 2012

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

FORM 10-Q

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

For the quarterly period ended September 30, 2012

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 1-3579

PITNEY BOWES INC.

(Exact name of registrant as specified in its charter)

Delaware 06-0495050  
(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)  
organization)

1 Elmcroft Road, Stamford, Connecticut 06926-0700  
(Address of principal executive offices) (Zip Code)  
(203) 356-5000  
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)  
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  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  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  Accelerated filer  Non-accelerated filer  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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of November 1, 2012.

Class Outstanding  
Common Stock, \$1 par value per share 200,751,672 shares

PITNEY BOWES INC.  
INDEX

|  | Page Number |
|--|-------------|
| <u>Part I - Financial Information:</u>   |             |
| <u>Item 1: Financial Statements (Unaudited)</u>  |             |
| <u>Condensed Consolidated Statements of Income for the Three and Nine Months Ended September 30, 2012 and 2011</u>               | <u>3</u>    |
| <u>Condensed Consolidated Statements of Comprehensive Income for the Three and Nine Months Ended September 30, 2012 and 2011</u> | <u>4</u>    |
| <u>Condensed Consolidated Balance Sheets at September 30, 2012 and December 31, 2011</u>   | <u>5</u>    |
| <u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2012 and 2011</u>                     | <u>6</u>    |
| <u>Notes to Condensed Consolidated Financial Statements</u>  | <u>7</u>    |
| <u>Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                             | <u>26</u>   |
| <u>Item 3: Quantitative and Qualitative Disclosures about Market Risk</u>  | <u>35</u>   |
| <u>Item 4: Controls and Procedures</u>   | <u>35</u>   |
| <u>Part II - Other Information:</u>  |             |
| <u>Item 1: Legal Proceedings</u>   | <u>36</u>   |
| <u>Item 1A: Risk Factors</u>   | <u>36</u>   |
| <u>Item 2: Unregistered Sales of Equity Securities and Use of Proceeds</u>   | <u>36</u>   |
| <u>Item 6: Exhibits</u>  | <u>36</u>   |
| <u>Signatures</u>  | <u>37</u>   |

## PART I. FINANCIAL INFORMATION

## Item 1: Financial Statements

## PITNEY BOWES INC.

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited; in thousands, except per share data)

|  | Three Months Ended |           | Nine Months Ended |           |
|--|--------------------|-----------|-------------------|-----------|
|  | September 30,      |           | September 30,     |           |
|  | 2012               | 2011      | 2012              | 2011      |
| Revenue:   |                    |           |                   |           |
| Equipment sales  | \$212,103          | \$221,475 | \$656,517         | \$706,027 |
| Supplies   | 66,902             | 74,271    | 213,789           | 235,728   |
| Software   | 93,476             | 113,224   | 302,377           | 318,305   |
| Rentals  | 142,288            | 154,210   | 428,174           | 467,064   |
| Financing  | 123,999            | 136,000   | 373,695           | 412,958   |
| Support services   | 171,652            | 175,286   | 516,424           | 530,707   |
| Business services  | 405,257            | 425,258   | 1,226,175         | 1,266,478 |
| Total revenue  | 1,215,677          | 1,299,724 | 3,717,151         | 3,937,267 |
| Costs and expenses:  |                    |           |                   |           |
| Cost of equipment sales  | 105,556            | 97,559    | 309,190           | 316,697   |
| Cost of supplies   | 20,694             | 22,611    | 65,428            | 74,365    |
| Cost of software   | 22,784             | 23,431    | 68,281            | 73,541    |
| Cost of rentals  | 25,182             | 35,819    | 87,257            | 107,834   |
| Financing interest expense   | 19,604             | 21,430    | 61,385            | 66,915    |
| Cost of support services   | 107,095            | 114,074   | 334,304           | 344,767   |
| Cost of business services  | 315,830            | 326,415   | 948,359           | 985,232   |
| Selling, general and administrative  | 400,862            | 427,412   | 1,203,653         | 1,286,739 |
| Research and development   | 36,669             | 35,573    | 104,518           | 107,772   |
| Restructuring charges and asset impairments  | 9,986              | 32,956    | 11,060            | 63,974    |
| Goodwill impairment  | 18,315             | 45,650    | 18,315            | 45,650    |
| Other interest expense   | 27,541             | 28,932    | 87,261            | 86,006    |
| Interest income  | (2,057)            | (1,265)   | (5,793)           | (4,702)   |
| Other expense (income), net  | —                  | (10,718)  | 1,138             | (10,718)  |
| Total costs and expenses   | 1,108,061          | 1,199,879 | 3,294,356         | 3,544,072 |
| Income from continuing operations before income taxes                                    | 107,616            | 99,845    | 422,795           | 393,195   |
| Provision (benefit) for income taxes   | 26,489             | (17,087)  | 93,519            | 77,319    |
| Income from continuing operations  | 81,127             | 116,932   | 329,276           | 315,876   |
| Income from discontinued operations, net of tax  | —                  | 60,428    | 19,332            | 57,911    |
| Net income before attribution of noncontrolling interests                                | 81,127             | 177,360   | 348,608           | 373,787   |
| Less: Preferred stock dividends of subsidiaries attributable to noncontrolling interests | 4,594              | 4,593     | 13,782            | 13,781    |
| Net income - Pitney Bowes Inc.   | \$76,533           | \$172,767 | \$334,826         | \$360,006 |
| Amounts attributable to common stockholders:   |                    |           |                   |           |
| Net income from continuing operations  | \$76,533           | \$112,339 | \$315,494         | \$302,095 |
| Income from discontinued operations, net of tax  | —                  | 60,428    | 19,332            | 57,911    |
| Net income - Pitney Bowes Inc.   | \$76,533           | \$172,767 | \$334,826         | \$360,006 |

Basic earnings per share attributable to common stockholders (1):

|                                |        |        |        |        |
|--------------------------------|--------|--------|--------|--------|
| Continuing operations          | \$0.38 | \$0.56 | \$1.58 | \$1.49 |
| Discontinued operations        | —      | 0.30   | 0.10   | 0.29   |
| Net income - Pitney Bowes Inc. | \$0.38 | \$0.86 | \$1.67 | \$1.78 |

Diluted earnings per share attributable to common stockholders (1):

|                                |        |        |        |        |
|--------------------------------|--------|--------|--------|--------|
| Continuing operations          | \$0.38 | \$0.56 | \$1.57 | \$1.48 |
| Discontinued operations        | —      | 0.30   | 0.10   | 0.28   |
| Net income - Pitney Bowes Inc. | \$0.38 | \$0.85 | \$1.66 | \$1.77 |

(1) The sum of the earnings per share amounts may not equal the totals due to rounding.

See Notes to Condensed Consolidated Financial Statements

PITNEY BOWES INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
 (Unaudited; in thousands)

|   | Three Months Ended<br>September 30, |            | Nine Months Ended<br>September 30, |           |
|---|-------------------------------------|------------|------------------------------------|-----------|
|   | 2012                                | 2011       | 2012                               | 2011      |
| Net income - Pitney Bowes Inc.  | \$76,533                            | \$172,767  | \$334,826                          | \$360,006 |
| Other comprehensive income, net of tax:   |                                     |            |                                    |           |
| Foreign currency translations   | 19,025                              | (111,317 ) | (883 )                             | (35,336 ) |
| Net unrealized gain on cash flow hedges, net of tax of \$21, \$773, \$374 and \$1,018, respectively                   | 25                                  | 1,209      | 578                                | 1,596     |
| Net unrealized gain on investment securities, net of tax of \$377, \$2,012, \$618 and \$2,722, respectively           | 589                                 | 3,147      | 967                                | 4,258     |
| Amortization of pension and postretirement costs, net of tax of \$6,755, \$4,825, \$20,221 and \$14,658, respectively | 12,151                              | 8,692      | 35,115                             | 25,857    |
| Other comprehensive income (loss)   | 31,790                              | (98,269 )  | 35,777                             | (3,625 )  |
| Comprehensive income - Pitney Bowes Inc.  | 108,323                             | 74,498     | 370,603                            | 356,381   |
| Preferred stock dividends of subsidiaries attributable to noncontrolling interests                                    | 4,594                               | 4,593      | 13,782                             | 13,781    |
| Total comprehensive income  | \$112,917                           | \$79,091   | \$384,385                          | \$370,162 |

See Notes to Condensed Consolidated Financial Statements

4

---

PITNEY BOWES INC.  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (Unaudited; in thousands, except share and per share data)

|   | September 30,<br>2012 | December 31,<br>2011 |
|---|-----------------------|----------------------|
| <b>ASSETS</b>   |                       |                      |
| Current assets:   |                       |                      |
| Cash and cash equivalents   | \$424,789             | \$856,238            |
| Short-term investments  | 36,238                | 12,971               |
| Accounts receivable, gross  | 695,575               | 755,485              |
| Allowance for doubtful accounts receivables                                     | (28,355)              | (31,855)             |
| Accounts receivable, net  | 667,220               | 723,630              |
| Finance receivables   | 1,218,080             | 1,296,673            |
| Allowance for credit losses   | (26,368)              | (45,583)             |
| Finance receivables, net  | 1,191,712             | 1,251,090            |
| Inventories   | 187,082               | 178,599              |
| Current income taxes  | 22,044                | 102,556              |
| Other current assets and prepayments  | 144,987               | 134,774              |
| Total current assets  | 2,674,072             | 3,259,858            |
| Property, plant and equipment, net  | 382,850               | 404,146              |
| Rental property and equipment, net  | 249,310               | 258,711              |
| Finance receivables   | 1,047,411             | 1,123,638            |
| Allowance for credit losses   | (18,235)              | (17,847)             |
| Finance receivables, net  | 1,029,176             | 1,105,791            |
| Investment in leveraged leases  | 34,373                | 138,271              |
| Goodwill  | 2,127,114             | 2,147,088            |
| Intangible assets, net  | 175,995               | 212,603              |
| Non-current income taxes  | 45,615                | 89,992               |
| Other assets  | 555,661               | 530,644              |
| Total assets  | \$7,274,166           | \$8,147,104          |
| <b>LIABILITIES, NONCONTROLLING INTERESTS AND STOCKHOLDERS' EQUITY (DEFICIT)</b> |                       |                      |
| Current liabilities:  |                       |                      |
| Accounts payable and accrued liabilities  | \$1,643,395           | \$1,840,465          |
| Current income taxes  | 220,236               | 242,972              |
| Notes payable and current portion of long-term obligations                      | 375,000               | 550,000              |
| Advance billings  | 449,051               | 458,425              |
| Total current liabilities   | 2,687,682             | 3,091,862            |
| Deferred taxes on income  | 25,017                | 175,944              |
| Tax uncertainties and other income tax liabilities                              | 193,867               | 194,840              |
| Long-term debt  | 3,305,504             | 3,683,909            |
| Other non-current liabilities   | 641,093               | 743,165              |
| Total liabilities   | 6,853,163             | 7,889,720            |
| Noncontrolling interests (Preferred stockholders' equity in subsidiaries)       | 296,370               | 296,370              |
| Commitments and contingencies (See Note 11)                                     |                       |                      |
| Stockholders' equity (deficit):   |                       |                      |
| Cumulative preferred stock, \$50 par value, 4% convertible                      | 4                     | 4                    |
| Cumulative preference stock, no par value, \$2.12 convertible                   | 653                   | 659                  |

Edgar Filing: PITNEY BOWES INC /DE/ - Form 10-Q

|  |             |              |   |
|--|-------------|--------------|---|
| Common stock, \$1 par value (480,000,000 shares authorized; 323,337,912 shares issued) | 323,338     | 323,338      |   |
| Additional paid-in capital   | 222,620     | 240,584      |   |
| Retained earnings  | 4,709,761   | 4,600,217    |   |
| Accumulated other comprehensive loss   | (625,868    | ) (661,645   | ) |
| Treasury stock, at cost (122,592,062 and 123,586,842 shares, respectively)             | (4,505,875  | ) (4,542,143 | ) |
| Total Pitney Bowes Inc. stockholders' equity (deficit)                                 | 124,633     | (38,986      | ) |
| Total liabilities, noncontrolling interests and stockholders' equity (deficit)         | \$7,274,166 | \$8,147,104  |   |
| See Notes to Condensed Consolidated Financial Statements                               |             |              |   |

5

---

PITNEY BOWES INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (Unaudited; in thousands)

|   | Nine Months Ended<br>September 30, |              |
|---|------------------------------------|--------------|
|   | 2012                               | 2011         |
| Cash flows from operating activities:   |                                    |              |
| Net income before attribution of noncontrolling interests                         | \$348,608                          | \$373,787    |
| Restructuring payments  | (60,746                            | ) (78,379 )  |
| Special pension plan contributions  | (95,000                            | ) (123,000 ) |
| Tax payments related to sale of leveraged lease assets                            | (99,249                            | ) —          |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                    |              |
| Goodwill impairment   | 18,315                             | 45,650       |
| Gain on sale of leveraged lease assets, net of tax                                | (12,886                            | ) (26,689 )  |
| Depreciation and amortization   | 191,507                            | 205,001      |
| Stock-based compensation  | 13,505                             | 13,393       |
| Restructuring charges and asset impairments                                       | 11,060                             | 63,974       |
| Changes in operating assets and liabilities:                                      |                                    |              |
| (Increase) decrease in accounts receivable  | 58,135                             | 113,422      |
| (Increase) decrease in finance receivables  | 144,442                            | 169,109      |
| (Increase) decrease in inventories  | (7,620                             | ) (12,731 )  |
| (Increase) decrease in other current assets and prepayments                       | (18,018                            | ) (3,707 )   |
| Increase (decrease) in accounts payable and accrued liabilities                   | (124,559                           | ) (102,092 ) |
| Increase (decrease) in current and non-current income taxes                       | 38,761                             | 133,893      |
| Increase (decrease) in advance billings   | (1,551                             | ) (22,392 )  |
| Increase (decrease) in other operating capital, net                               | 34,929                             | 1,217        |
| Net cash provided by operating activities   | 439,633                            | 750,456      |
| Cash flows from investing activities:   |                                    |              |
| Short-term and other investments  | (58,255                            | ) (100,268 ) |
| Capital expenditures  | (127,816                           | ) (123,029 ) |
| Proceeds from sale of leveraged lease assets                                      | 105,506                            | 101,784      |
| Net investment in external financing  | (134                               | ) (4,458 )   |
| Reserve account deposits  | (15,373                            | ) (14,528 )  |
| Net cash used in investing activities   | (96,072                            | ) (140,499 ) |
| Cash flows from financing activities:   |                                    |              |
| Decrease in notes payable, net  | —                                  | (50,000 )    |
| Principal payments of long-term obligations                                       | (550,000                           | ) —          |
| Proceeds from issuance of common stock  | 6,989                              | 10,436       |
| Stock repurchases   | —                                  | (99,997 )    |
| Dividends paid to stockholders  | (225,282                           | ) (225,676 ) |
| Dividends paid to noncontrolling interests  | (9,188                             | ) (9,188 )   |
| Net cash used in financing activities   | (777,481                           | ) (374,425 ) |
| Effect of exchange rate changes on cash and cash equivalents                      | 2,471                              | (4,701 )     |
| (Decrease) increase in cash and cash equivalents                                  | (431,449                           | ) 230,831    |
| Cash and cash equivalents at beginning of period                                  | 856,238                            | 484,363      |
| Cash and cash equivalents at end of period  | \$424,789                          | \$715,194    |
| Cash interest paid  | \$170,119                          | \$177,682    |
| Cash income tax payments (refund), net  | \$145,090                          | \$(68,659 )  |

See Notes to Condensed Consolidated Financial Statements

6

---

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 1. Description of Business and Basis of Presentation

Pitney Bowes Inc. and its subsidiaries (the company, we, us, and our) is a global provider of software, hardware and services that enables both physical and digital communications and that integrates those physical and digital communications channels. We offer a full suite of equipment, supplies, software, services and solutions for managing and integrating physical and digital communication channels. We conduct our business activities in seven reporting segments within two business groups: Small & Medium Business Solutions and Enterprise Business Solutions. See Note 12 for information regarding our reportable segments.

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and the instructions to Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In addition, the December 31, 2011 Condensed Consolidated Balance Sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. In management's opinion, all adjustments, consisting of normal recurring adjustments, considered necessary to present fairly our financial position, results of operations and cash flows for the periods presented have been included. Operating results for the periods presented are not necessarily indicative of the results that may be expected for any other interim period or the year ending December 31, 2012.

These statements should be read in conjunction with the financial statements and notes thereto included in our Annual Report to Stockholders on Form 10-K for the year ended December 31, 2011 (the 2011 Annual Report). Certain prior year amounts have been reclassified to conform to the current period presentation.

## 2. Inventories

Inventories at September 30, 2012 and December 31, 2011 consisted of the following:

|                                    | September 30,<br>2012 | December 31,<br>2011 |
|------------------------------------|-----------------------|----------------------|
| Raw materials and work in process  | \$64,333              | \$63,216             |
| Supplies and service parts         | 75,053                | 68,600               |
| Finished products                  | 74,653                | 71,958               |
| Inventory at FIFO cost             | 214,039               | 203,774              |
| Excess of FIFO cost over LIFO cost | (26,957 )             | (25,175 )            |
| Total inventory, net               | \$187,082             | \$178,599            |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 3. Finance Assets

## Finance Receivables

Finance receivables are comprised of sales-type lease receivables and unsecured revolving loan receivables.

Sales-type lease receivables are generally due in monthly, quarterly or semi-annual installments over periods ranging from three to five years. Loan receivables arise primarily from financing services offered to our customers for postage and related supplies. Loan receivables are generally due each month; however, customers may rollover outstanding balances.

Finance receivables at September 30, 2012 and December 31, 2011 consisted of the following:

|  | September 30, 2012 |               |              |
|--|--------------------|---------------|--------------|
|  | North America      | International | Total        |
| Sales-type lease receivables                   |                    |               |              |
| Gross finance receivables                      | \$ 1,603,444       | \$ 456,370    | \$ 2,059,814 |
| Unguaranteed residual values                   | 155,999            | 20,733        | 176,732      |
| Unearned income                                | (317,457)          | (105,525)     | (422,982)    |
| Allowance for credit losses                    | (17,138)           | (9,820)       | (26,958)     |
| Net investment in sales-type lease receivables | 1,424,848          | 361,758       | 1,786,606    |
| Loan receivables                               |                    |               |              |
| Loan receivables                               | 404,099            | 47,848        | 451,947      |
| Allowance for credit losses                    | (15,477)           | (2,188)       | (17,665)     |
| Net investment in loan receivables             | 388,622            | 45,660        | 434,282      |
| Net investment in finance receivables          | \$ 1,813,470       | \$ 407,418    | \$ 2,220,888 |
|  |                    |               |              |
|  | December 31, 2011  |               |              |
|  | North America      | International | Total        |
| Sales-type lease receivables                   |                    |               |              |
| Gross finance receivables                      | \$ 1,727,653       | \$ 460,101    | \$ 2,187,754 |
| Unguaranteed residual values                   | 185,450            | 20,443        | 205,893      |
| Unearned income                                | (348,286)          | (102,618)     | (450,904)    |
| Allowance for credit losses                    | (28,661)           | (12,039)      | (40,700)     |
| Net investment in sales-type lease receivables | 1,536,156          | 365,887       | 1,902,043    |
| Loan receivables                               |                    |               |              |
| Loan receivables                               | 436,631            | 40,937        | 477,568      |
| Allowance for credit losses                    | (20,272)           | (2,458)       | (22,730)     |
| Net investment in loan receivables             | 416,359            | 38,479        | 454,838      |
| Net investment in finance receivables          | \$ 1,952,515       | \$ 404,366    | \$ 2,356,881 |

## Allowance for Credit Losses and Aging of Receivables

We estimate our finance receivable risks and provide allowances for credit losses accordingly. We establish credit approval limits based on the credit quality of the customer and the type of equipment financed. We believe that our concentration of credit risk is limited because of our large number of customers, small account balances for most of our customers, and customer geographic and industry diversification.

Our policy is to discontinue revenue recognition for lease receivables that are more than 120 days past due and for unsecured loan receivables that are more than 90 days past due. We resume revenue recognition when customer payments reduce the account balance aging to 60 days or less past due. We evaluate the adequacy of the allowance for credit losses based on historical loss experience, the nature and volume of our portfolios, adverse situations that may affect a customer's ability to pay and prevailing economic conditions, and make adjustments to the reserves as necessary. This evaluation is inherently subjective and actual results may differ significantly from estimated reserves.



## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

We maintain a program for U.S. borrowers in our North America loan portfolio who are experiencing financial difficulties, but are able to make reduced payments over an extended period of time. Upon acceptance into the program, the borrower's credit line is closed, interest accrual is suspended, the borrower's minimum required payment is reduced and the account is re-aged and classified as current. There is generally no forgiveness of debt or reduction of balances owed. The loans in the program are considered to be troubled debt restructurings because of the concessions granted to the borrower. At September 30, 2012 and December 31, 2011, loans in this program had a balance of \$5 million and \$7 million, respectively.

The allowance for credit losses for these modified loans is determined by the difference between the cash flows expected to be received from the borrower discounted at the original effective rate and the carrying value of the loan. The allowance for credit losses related to such loans was \$1 million at September 30, 2012 and \$2 million at December 31, 2011 and is included in the allowance for credit losses of North America loans in the table below. Management believes that the allowance for credit losses is adequate for these loans and all other loans in the portfolio. Write-offs of loans in the program for the past twelve months were less than \$1 million.

Activity in the allowance for credit losses for finance receivables for the nine months ended September 30, 2012 was as follows:

|                               | Sales-type Lease Receivables |               | Loan Receivables |               |          |
|-------------------------------|------------------------------|---------------|------------------|---------------|----------|
|                               | North America                | International | North America    | International | Total    |
| Balance at January 1, 2012    | \$28,661                     | \$12,039      | \$20,272         | \$2,458       | \$63,430 |
| Amounts charged to expense    | 1,171                        | 1,489         | 4,069            | 703           | 7,432    |
| Accounts written off          | (12,694)                     | (3,708)       | (8,864)          | (973)         | (26,239) |
| Balance at September 30, 2012 | \$17,138                     | \$9,820       | \$15,477         | \$2,188       | \$44,623 |

The aging of finance receivables at September 30, 2012 and December 31, 2011 was as follows:

|                            | Sales-type Lease Receivables |               | Loan Receivables |               |             |
|----------------------------|------------------------------|---------------|------------------|---------------|-------------|
|                            | North America                | International | North America    | International | Total       |
| September 30, 2012         |                              |               |                  |               |             |
| < 31 days                  | \$1,520,139                  | \$429,389     | \$382,897        | \$42,549      | \$2,374,974 |
| > 30 days and < 61 days    | 30,160                       | 8,996         | 11,268           | 3,451         | 53,875      |
| > 60 days and < 91 days    | 29,187                       | 5,444         | 4,302            | 1,211         | 40,144      |
| > 90 days and < 121 days   | 6,441                        | 3,118         | 2,280            | 347           | 12,186      |
| > 120 days                 | 17,517                       | 9,423         | 3,352            | 290           | 30,582      |
| Total                      | \$1,603,444                  | \$456,370     | \$404,099        | \$47,848      | \$2,511,761 |
| Past due amounts > 90 days |                              |               |                  |               |             |
| Still accruing interest    | \$6,441                      | \$3,118       | \$—              | \$—           | \$9,559     |
| Not accruing interest      | 17,517                       | 9,423         | 5,632            | 637           | 33,209      |
| Total                      | \$23,958                     | \$12,541      | \$5,632          | \$637         | \$42,768    |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

|                            | Sales-type Lease Receivables |               | Loan Receivables |               | Total       |
|----------------------------|------------------------------|---------------|------------------|---------------|-------------|
|                            | North America                | International | North America    | International |             |
| December 31, 2011          |                              |               |                  |               |             |
| < 31 days                  | \$1,641,706                  | \$434,811     | \$414,434        | \$38,841      | \$2,529,792 |
| > 30 days and < 61 days    | 41,018                       | 10,152        | 12,399           | 1,066         | 64,635      |
| > 60 days and < 91 days    | 24,309                       | 5,666         | 4,362            | 425           | 34,762      |
| > 90 days and < 121 days   | 4,912                        | 3,207         | 2,328            | 186           | 10,633      |
| > 120 days                 | 15,708                       | 6,265         | 3,108            | 419           | 25,500      |
| Total                      | \$1,727,653                  | \$460,101     | \$436,631        | \$40,937      | \$2,665,322 |
| Past due amounts > 90 days |                              |               |                  |               |             |
| Still accruing interest    | \$4,912                      | \$3,207       | \$—              | \$—           | \$8,119     |
| Not accruing interest      | 15,708                       | 6,265         | 5,436            | 605           | 28,014      |
| Total                      | \$20,620                     | \$9,472       | \$5,436          | \$605         | \$36,133    |

## Credit Quality

The extension of credit and management of credit lines to new and existing customers uses a combination of an automated credit score, where available, and a detailed manual review of the customer's financial condition and, when applicable, the customer's payment history. Once credit is granted, the payment performance of the customer is managed through automated collections processes and is supplemented with direct follow up should an account become delinquent. We have robust automated collections and extensive portfolio management processes. The portfolio management processes ensure that our global strategy is executed, collection resources are allocated appropriately and enhanced tools and processes are implemented as needed.

We use a third party to score the majority of the North America portfolio on a quarterly basis using a commercial credit score. We do not use a third party to score our International portfolios because the cost to do so is prohibitive, it is a localized process and there is no single credit score model that covers all countries.

The table below shows the North America portfolio at September 30, 2012 and December 31, 2011 by relative risk class (low, medium, high) based on the relative scores of the accounts within each class. The relative scores are determined based on a number of factors, including the company type, ownership structure, payment history and financial information. A fourth class is shown for accounts that are not scored. Absence of a score is not indicative of the credit quality of the account. The degree of risk, as defined by the third party, refers to the relative risk that an account in the next 12 month period may become delinquent.

• Low risk accounts are companies with very good credit scores and are considered to approximate the top 30% of all commercial borrowers.

• Medium risk accounts are companies with average to good credit scores and are considered to approximate the middle 40% of all commercial borrowers.

• High risk accounts are companies with poor credit scores, are delinquent or are at risk of becoming delinquent and are considered to approximate the bottom 30% of all commercial borrowers.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

|                              | September 30,<br>2012 | December 31,<br>2011 |
|------------------------------|-----------------------|----------------------|
| Sales-type lease receivables |                       |                      |
| Risk Level                   |                       |                      |
| Low                          | \$1,070,643           | \$1,096,676          |
| Medium                       | 416,138               | 473,394              |
| High                         | 50,222                | 58,177               |
| Not Scored                   | 66,441                | 99,406               |
| Total                        | \$1,603,444           | \$1,727,653          |
| Loan receivables             |                       |                      |
| Risk Level                   |                       |                      |
| Low                          | \$258,849             | \$269,547            |
| Medium                       | 126,984               | 115,490              |
| High                         | 15,114                | 21,081               |
| Not Scored                   | 3,152                 | 30,513               |
| Total                        | \$404,099             | \$436,631            |

Although the relative score of accounts within each class is used as a factor in determining a customer credit limit, it is not indicative of our actual history of losses due to the business essential nature of our products and services. The aging schedule included above, showing approximately 1.7% of the portfolio as greater than 90 days past due, and the roll-forward schedule of the allowance for credit losses, showing the actual losses for the nine months ended September 30, 2012, are more representative of the potential loss performance of our portfolio than relative risk based on scores, as defined by the third party.

## Leveraged Leases

Our investment in leveraged lease assets consisted of the following:

|  | September 30,<br>2012 | December 31,<br>2011 |
|--|-----------------------|----------------------|
| Rental receivables                               | \$89,193              | \$810,306            |
| Unguaranteed residual values                     | 14,312                | 13,784               |
| Principal and interest on non-recourse loans     | (60,762               | ) (606,708           |
| Unearned income                                  | (8,370                | ) (79,111            |
| Investment in leveraged leases                   | 34,373                | 138,271              |
| Less: deferred taxes related to leveraged leases | (20,199               | ) (101,255           |
| Net investment in leveraged leases               | \$14,174              | \$37,016             |

The following is a summary of the components of income from leveraged leases:

|                               | Three Months Ended |         | Nine Months Ended |         |
|-------------------------------|--------------------|---------|-------------------|---------|
|                               | September 30,      |         | September         |         |
|                               | 2012               | 2011    | 2012              | 2011    |
| Pretax leveraged lease income | \$467              | \$1,457 | \$1,692           | \$4,551 |
| Income tax effect             | 8                  | (641    | ) 33              | (804    |
| Income from leveraged leases  | \$475              | \$816   | \$1,725           | \$3,747 |

During 2012, we sold certain non-U.S. leveraged lease assets for cash. The investment in the leveraged lease assets at the date of sale was \$109 million and an after-tax gain of \$13 million was recognized. In the third quarter 2011, we also sold certain non-U.S. leveraged lease assets for cash. The investment in the leveraged lease assets at the date of sale was \$109 million and an after-tax gain of \$27 million was recognized. The effects of these sales are not included in the table above.



## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 4. Intangible Assets and Goodwill

## Intangible assets

Intangible assets at September 30, 2012 and December 31, 2011 consisted of the following:

|                          | September 30, 2012    |                          |                     | December 31, 2011     |                          |                     |
|--------------------------|-----------------------|--------------------------|---------------------|-----------------------|--------------------------|---------------------|
|                          | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
| Customer relationships   | \$406,746             | \$(260,737)              | \$146,009           | \$409,489             | \$(237,536)              | \$171,953           |
| Supplier relationships   | 29,000                | (21,387)                 | 7,613               | 29,000                | (19,213)                 | 9,787               |
| Software & technology    | 168,912               | (149,360)                | 19,552              | 170,286               | (143,456)                | 26,830              |
| Trademarks & trade names | 34,844                | (32,101)                 | 2,743               | 33,908                | (30,076)                 | 3,832               |
| Non-compete agreements   | 7,487                 | (7,409)                  | 78                  | 7,564                 | (7,363)                  | 201                 |
| Total intangible assets  | \$646,989             | \$(470,994)              | \$175,995           | \$650,247             | \$(437,644)              | \$212,603           |

Amortization expense for intangible assets was \$10 million and \$14 million for the three months ended September 30, 2012 and 2011, respectively, and \$35 million and \$43 million for the nine months ended September 30, 2012 and 2011, respectively. We also recorded impairment charges of \$3 million to write-down the carrying values of certain intangible assets associated with our International Mail Services business to their respective fair values. See Goodwill section below for further details of the impairment charge and method of determining fair value.

The future amortization expense for intangible assets as of September 30, 2012 was as follows:

|  |           |
|--|-----------|
| Remaining for year ended December 31, 2012 | \$10,222  |
| Year ended December 31, 2013               | 39,429    |
| Year ended December 31, 2014               | 36,774    |
| Year ended December 31, 2015               | 32,812    |
| Year ended December 31, 2016               | 24,182    |
| Thereafter                                 | 32,576    |
| Total                                      | \$175,995 |

Actual amortization expense may differ from the amounts above due to, among other things, fluctuations in foreign currency exchange rates, impairments, future acquisitions and accelerated amortization.

## Goodwill

We perform our annual goodwill impairment test during the fourth quarter of each year, or sooner, if circumstances indicate an impairment may exist. Based on the recent performance of our International Mail Services (IMS) business and to enable us to better focus on higher growth cross-border ecommerce parcel opportunities, in the third quarter of 2012, we began exploring strategic alternatives for the IMS business. In October 2012, we made a strategic decision to exit the IMS business related to the international delivery of mail and catalogs. We are engaged in negotiations with potential buyers and have received preliminary indications of interest and written offers. As a result of these factors, we concluded that it was more likely than not that the fair value of the IMS reporting unit was below its book value and an interim impairment test was performed. The fair value of the reporting unit was determined in combination of the written offers received as well as applying an income approach with revised cash flow projections. The inputs used to determine the fair value of the IMS business are classified as Level 3 in the fair value hierarchy. Based on the results of our impairment test, a non-cash goodwill impairment charge of \$18 million was recorded in the third quarter of 2012 to write-down the carrying value of goodwill associated with the IMS business to its implied fair value.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

The changes in the carrying amount of goodwill, by reporting segment, for the nine months ended September 30, 2012 were as follows:

|                                      | Gross value<br>before<br>accumulated<br>impairment | Accumulated<br>impairment | December 31,<br>2011 | Impairment  | Other (1)  | September 30,<br>2012 |
|--------------------------------------|--|---------------------------|----------------------|-------------|------------|-----------------------|
| North America Mailing                | \$ 352,897   | \$ —                      | \$ 352,897           | \$—         | \$(178 )   | \$ 352,719            |
| International Mailing                | 189,067  | —                         | 189,067              | —           | (8,105 )   | 180,962               |
| Small & Medium Business<br>Solutions | 541,964  | —                         | 541,964              | —           | (8,283 )   | 533,681               |
| Production Mail                      | 127,589  | —                         | 127,589              | —           | 2,603      | 130,192               |
| Software                             | 667,124  | —                         | 667,124              | —           | 3,479      | 670,603               |
| Management Services                  | 487,223  | (84,500 )                 | 402,723              | —           | 542        | 403,265               |
| Mail Services                        | 259,105  | (45,650 )                 | 213,455              | (18,315 )   | —          | 195,140               |
| Marketing Services                   | 194,233  | —                         | 194,233              | —           | —          | 194,233               |
| Enterprise Business Solutions        | 1,735,274  | (130,150 )                | 1,605,124            | (18,315 )   | 6,624      | 1,593,433             |
| Total                                | \$ 2,277,238                                       | \$ (130,150 )             | \$ 2,147,088         | \$(18,315 ) | \$(1,659 ) | \$ 2,127,114          |

(1) Primarily foreign currency translation adjustments.

## 5. Debt

In March 2012, we redeemed, at par plus accrued interest, a \$150 million term loan that was scheduled to mature in the fourth quarter of 2012.

In April 2012, we entered into forward starting swap agreements with an aggregate notional value of \$150 million to hedge the interest rate risk associated with the forecasted issuance of long-term debt. The anticipated debt issuance did not occur prior to the expiration of these swap agreements and a loss of \$6 million was recognized in the second quarter of 2012.

In June 2012, we redeemed our \$400 million, 4.625% notes (the 2012 Notes) that were scheduled to mature in October 2012. As a result of the early redemption of the 2012 Notes, we recorded a net loss of \$2 million on the extinguishment of debt.

At September 30, 2012, there were no outstanding commercial paper borrowings. During the quarter, commercial paper borrowings averaged \$418 million at a weighted-average interest rate of 0.48% and the maximum amount outstanding at any time was \$709 million.

In October 2012, we borrowed \$220 million under term loan agreements. The loans bear interest at the applicable London Interbank Offered Rate (LIBOR) plus 2.25% or Prime Rate plus 1.25%, at our option. Interest is payable quarterly and the loans mature in 2015 and 2016. The proceeds from the loans will be used for general corporate purposes, including the repayment of commercial paper and 2013 debt maturities.

## 6. Noncontrolling Interests (Preferred Stockholders' Equity in Subsidiaries)

Pitney Bowes International Holdings, Inc. (PBIH), a subsidiary, has 300,000 shares, or \$300 million, of outstanding perpetual voting preferred stock (the Preferred Stock) held by certain institutional investors. The holders of the Preferred Stock are entitled as a group to 25% of the combined voting power of all classes of capital stock of PBIH. All outstanding common stock of PBIH, representing the remaining 75% of the combined voting power of all classes of capital stock, is owned directly or indirectly by the company. The Preferred Stock is entitled to cumulative dividends at a rate of 6.125% through 2016 after which it becomes callable and, if it remains outstanding, will yield a dividend that increases by 50% every six months thereafter. No dividends were in arrears at September 30, 2012 or December 31, 2011. There was no change in the carrying value of noncontrolling interests during the period ended September 30, 2012 or the year ended December 31, 2011.



PITNEY BOWES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

7. Income Taxes

The effective tax rate for the three months ended September 30, 2012 and 2011 was 24.6% and (17.1)%, respectively. The effective tax rate for the three months ended September 30, 2012 includes tax benefits of \$36 million from the resolution of tax examinations and tax accruals of \$28 million for the repatriation of non-U.S. earnings. The effective tax rate for the three months ended September 30, 2011 includes tax benefits of \$34 million from the sale of non-U.S. leveraged lease assets and \$18 million from the resolution of tax examinations.

The effective tax rate for the nine months ended September 30, 2012 and 2011 was 22.1% and 19.7%, respectively. The effective tax rate for the nine months ended September 30, 2012 include tax benefits of \$17 million from the sale of non-U.S. leveraged lease assets (net of \$15 million of tax accrued to repatriate these earnings), \$58 million from the resolution of tax examinations, and tax accruals of \$28 million for the repatriation of additional non-U.S. earnings. The effective tax rate for the nine months ended September 30, 2011 includes the tax benefit of \$34 million from the sale of non-U.S. leveraged lease assets and \$27 million from the resolution of tax examinations.

With the exception of the impact of unusual sales of leveraged lease assets and the one-time restructuring of our Canadian operations that led us to accrue taxes for the repatriation of certain earnings, it is our intention to permanently reinvest substantially all of our foreign cash in our foreign operations.

On August 27, 2012, the Third Circuit Court of Appeals overturned a prior Tax Court decision and ruled in favor of the IRS and adverse to the Historic Boardwalk Hall LLC, a partnership in which we had made an investment in 2000. The judgment is not yet final. Based on our partnership contractual relationship, we do not expect this matter to have a material effect on our financial position or results of operations.

As is the case with other large corporations, our tax returns are examined each year by tax authorities in the United States, other countries and local jurisdictions in which we have operations. Except for issues arising out of certain partnership investments, the IRS examination of tax years 2001-2004 is closed to audit and the examination of years 2005-2008 is expected to be closed to audit by the end of 2012. Other significant tax filings subject to examination include various post-2000 U.S. state and local, post 2007 Canadian and German, and post-2008 French and U.K. tax filings. We have other less significant tax filings currently under examination or subject to examination.

We regularly assess the likelihood of tax adjustments in each of the tax jurisdictions in which we have operations and account for the related financial statement implications. We believe we have established tax reserves that are appropriate given the possibility of tax adjustments. However, determining the appropriate level of tax reserves requires judgment regarding the uncertain application of tax law and the possibility of tax adjustments. Future changes in tax reserve requirements could have a material impact, positive or negative, on our results of operations, financial position and cash flows.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 8. Stockholders' Equity

Changes in stockholders' equity for the nine months ended September 30, 2012 and 2011 were as follows:

|                                  | Preferred<br>stock | Preference<br>stock | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>earnings | Accumulated<br>other<br>comprehensive<br>loss | Treasury<br>stock | Total<br>equity |
|----------------------------------|--------------------|---------------------|-----------------|----------------------------------|----------------------|---|-------------------|-----------------|
| Balance at January 1, 2012       | \$4                | \$659               | \$323,338       | \$240,584                        | \$4,600,217          | \$ (661,645 )                                 | \$(4,542,143)     | \$(38,986 )     |
| Net income                       | —                  | —                   | —               | —                                | 334,826              | —   | —                 | 334,826         |
| Other comprehensive income       | —                  | —                   | —               | —                                | —                    | 35,777  | —                 | 35,777          |
| Cash dividends                   |                    |                     |                 |                                  |                      |   |                   |                 |
| Common (\$1.125 per share)       | —                  | —                   | —               | —                                | (225,244 )           | —   | —                 | (225,244 )      |
| Preference                       | —                  | —                   | —               | —                                | (38 )                | —   | —                 | (38 )           |
| Issuances of common stock        | —                  | —                   | —               | (31,306 )                        | —                    | —   | 36,138            | 4,832           |
| Conversions to common stock      | —                  | (6 )                | —               | (124 )                           | —                    | —   | 130               | —               |
| Stock-based compensation expense | —                  | —                   | —               | 13,466                           | —                    | —   | —                 | 13,466          |
| Balance at September 30, 2012    | \$4                | \$653               | \$323,338       | \$222,620                        | \$4,709,761          | \$ (625,868 )                                 | \$(4,505,875)     | \$124,633       |

|                             | Preferred<br>stock | Preference<br>stock | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>earnings | Accumulated<br>other<br>comprehensive<br>loss | Treasury<br>stock | Total<br>equity |
|-----------------------------|--------------------|---------------------|-----------------|----------------------------------|----------------------|---|-------------------|-----------------|
| Balance at January 1, 2011  | \$4                | \$752               | \$323,338       | \$250,928                        | \$4,282,316          | \$ (473,806 )                                 | \$(4,480,113)     | \$(96,581 )     |
| Net income                  | —                  | —                   | —               | —                                | 360,006              | —   | —                 | 360,006         |
| Other comprehensive income  | —                  | —                   | —               | —                                | —                    | (3,625 )                                      | —                 | (3,625 )        |
| Cash dividends              |                    |                     |                 |                                  |                      |   |                   |                 |
| Common (\$1.11 per share)   | —                  | —                   | —               | —                                | (225,632 )           | —   | —                 | (225,632 )      |
| Preference                  | —                  | —                   | —               | —                                | (44 )                | —   | —                 | (44 )           |
| Issuances of common stock   | —                  | —                   | —               | (25,387 )                        | —                    | —   | 32,584            | 7,197           |
| Conversions to common stock | —                  | (28 )               | —               | (621 )                           | —                    | —   | 649               | —               |
|                             | —                  | —                   | —               | 13,393                           | —                    | —   | —                 | 13,393          |

|                                  |     |       |           |           |             |               |               |             |
|----------------------------------|-----|-------|-----------|-----------|-------------|---------------|---------------|-------------|
| Stock-based compensation expense |     |       |           |           |             |               |               |             |
| Repurchase of common stock       | —   | —     | —         | —         | —           |               | (99,997 )     | (99,997 )   |
| Balance at September 30, 2011    | \$4 | \$724 | \$323,338 | \$238,313 | \$4,416,646 | \$ (477,431 ) | \$(4,546,877) | \$(45,283 ) |

The components of accumulated other comprehensive loss at September 30, 2012 and 2011 were as follows:

|   | January 1, 2012 | Other comprehensive income | September 30, 2012 | January 1, 2011 | Other comprehensive income | September 30, 2011 |
|---|-----------------|----------------------------|--------------------|-----------------|----------------------------|--------------------|
| Foreign currency translation adjustments                        | \$83,952        | \$ (883 )                  | \$ 83,069          | \$137,521       | \$ (35,336 )               | \$ 102,185         |
| Net unrealized (loss) gain on derivatives                       | (8,438 )        | 578                        | (7,860 )           | (10,445 )       | 1,596                      | (8,849 )           |
| Net unrealized gain on investment securities                    | 4,387           | 967                        | 5,354              | 1,439           | 4,258                      | 5,697              |
| Net unamortized (loss) gain on pension and postretirement plans | (741,546 )      | 35,115                     | (706,431 )         | (602,321 )      | 25,857                     | (576,464 )         |
| Accumulated other comprehensive loss                            | \$(661,645)     | \$ 35,777                  | \$(625,868 )       | \$(473,806)     | \$ (3,625 )                | \$(477,431 )       |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 9. Fair Value Measurements and Derivative Instruments

We measure certain financial assets and liabilities at fair value on a recurring basis. Fair value is a market-based measure considered from the perspective of a market participant rather than an entity-specific measure. An entity is required to classify certain assets and liabilities measured at fair value based on the following fair value hierarchy that prioritizes the inputs used to measure fair value:

Level 1 – Unadjusted quoted prices in active markets for identical assets and liabilities.

Level 2 – Quoted prices for identical assets and liabilities in markets that are not active, quoted prices for similar assets and liabilities in active markets or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity, may be derived from internally developed methodologies based on management's best estimate of fair value and that are significant to the fair value of the asset or liability.

The following tables show, by level within the fair value hierarchy, our financial assets and liabilities that are accounted for at fair value on a recurring basis at September 30, 2012 and December 31, 2011. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment and may affect their placement within the fair value hierarchy.

|   | September 30, 2012 |            |         | Total       |
|---|--------------------|------------|---------|-------------|
|   | Level 1            | Level 2    | Level 3 |             |
| <b>Assets:</b>  |                    |            |         |             |
| Investment securities   |                    |            |         |             |
| Money market funds / commercial paper                                       | \$ 198,431         | \$ 20,717  | \$—     | \$ 219,148  |
| Equity securities   | —                  | 24,891     | —       | 24,891      |
| Commingled fixed income securities  | —                  | 29,286     | —       | 29,286      |
| Debt securities - U.S. and foreign governments, agencies and municipalities | 119,858            | 21,322     | —       | 141,180     |
| Debt securities - corporate   | —                  | 40,134     | —       | 40,134      |
| Mortgage-backed / asset-backed securities                                   | —                  | 143,631    | —       | 143,631     |
| Derivatives   |                    |            |         |             |
| Interest rate swaps   | —                  | 11,643     | —       | 11,643      |
| Foreign exchange contracts  | —                  | 1,187      | —       | 1,187       |
| Total assets  | \$ 318,289         | \$ 292,811 | \$—     | \$ 611,100  |
| <b>Liabilities:</b>   |                    |            |         |             |
| Derivatives   |                    |            |         |             |
| Foreign exchange contracts  | \$—                | \$ (5,434  | ) \$—   | \$ (5,434 ) |
| Total liabilities   | \$—                | \$ (5,434  | ) \$—   | \$ (5,434 ) |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

|   | December 31, 2011 |           |         | Total     |
|---|-------------------|-----------|---------|-----------|
|   | Level 1           | Level 2   | Level 3 |           |
| Assets:   |                   |           |         |           |
| Investment securities   |                   |           |         |           |
| Money market funds / commercial paper                                       | \$239,157         | \$300,702 | \$—     | \$539,859 |
| Equity securities   | —                 | 22,097    | —       | 22,097    |
| Commingled fixed income securities  | —                 | 27,747    | —       | 27,747    |
| Debt securities - U.S. and foreign governments, agencies and municipalities | 93,175            | 19,042    | —       | 112,217   |
| Debt securities - corporate   | —                 | 31,467    | —       | 31,467    |
| Mortgage-backed / asset-backed securities                                   | —                 | 134,262   | —       | 134,262   |
| Derivatives   |                   |           |         |           |
| Interest rate swaps   | —                 | 15,465    | —       | 15,465    |
| Foreign exchange contracts  | —                 | 4,230     | —       | 4,230     |
| Total assets  | \$332,332         | \$555,012 | \$—     | \$887,344 |
| Liabilities:  |                   |           |         |           |
| Derivatives   |                   |           |         |           |
| Foreign exchange contracts  | \$—               | \$(1,439) | \$—     | \$(1,439) |
| Total liabilities   | \$—               | \$(1,439) | \$—     | \$(1,439) |

## Investment Securities

The valuation of investment securities is based on the market approach using inputs that are observable, or can be corroborated by observable data, in an active marketplace. The following information relates to our classification into the fair value hierarchy:

**Money Market Funds / Commercial Paper:** Money market funds typically invest in government securities, certificates of deposit, commercial paper and other highly liquid and low-risk securities. Money market funds are principally used for overnight deposits and are classified as Level 1 when unadjusted quoted prices in active markets are available and as Level 2 when they are not actively traded on an exchange. Direct investments in commercial paper are not listed on an exchange in an active market and are classified as Level 2.

**Equity Securities:** Equity securities are comprised of mutual funds investing in U.S. and foreign common stock. These mutual funds are classified as Level 2 as they are not separately listed on an exchange.

**Commingled Fixed Income Securities:** Mutual funds that invest in a variety of fixed income securities including securities of the U.S. government and its agencies, corporate debt, mortgage-backed securities and asset-backed securities. The value of the funds is based on the market value of the underlying investments owned by each fund, minus its liabilities, divided by the number of shares outstanding, as reported by the fund manager. These commingled funds are not listed on an exchange in an active market and are classified as Level 2.

**Debt Securities – U.S. and Foreign Governments, Agencies and Municipalities:** Debt securities are classified as Level 1 where active, high volume trades for identical securities exist. Valuation adjustments are not applied to these securities. Debt securities valued using quoted market prices for similar securities or benchmarking model derived prices to quoted market prices and trade data for identical or comparable securities are classified as Level 2.

**Debt Securities – Corporate:** Corporate debt securities are valued using recently executed transactions, market price quotations where observable, or bond spreads. The spread data used are for the same maturity as the security. These securities are classified as Level 2.

**Mortgage-Backed Securities (MBS) / Asset-Backed Securities (ABS):** These securities are valued based on external pricing indices. When external index pricing is not observable, MBS and ABS are valued based on external price/spread data. These securities are classified as Level 2.

The carrying value of our investment securities at September 30, 2012 and December 31, 2011 was \$590 million and \$861 million, respectively.



## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

Investment securities include investments held by The Pitney Bowes Bank, a wholly owned subsidiary and a Utah-chartered Industrial Loan Company. The bank's investments at September 30, 2012 and December 31, 2011 were \$348 million and \$282 million, respectively. These investments are reported on the Condensed Consolidated Balance Sheets as cash and cash equivalents, short-term investments and other assets depending on the type of investment and maturity.

We have not experienced any write-offs in our investment portfolio. The majority of our MBS are either guaranteed or supported by the U.S. government. Market events have not caused our money market funds to experience declines in their net asset value below \$1.00 per share or to incur imposed limits on redemptions. We have no investments in inactive markets that would warrant a possible change in our pricing methods or classification within the fair value hierarchy. Further, we have no investments in auction rate securities.

## Derivative Instruments

In the normal course of business, we are exposed to the impact of interest rate changes and foreign currency fluctuations. We limit these risks by following established risk management policies and procedures, including the use of derivatives. We use derivatives to manage the related cost of debt and to limit the effects of foreign exchange rate fluctuations on financial results. We do not use derivatives for trading or speculative purposes. We record our derivative instruments at fair value, and the accounting for changes in the fair value of the derivatives depends on the intended use of the derivative, the resulting designation, and the effectiveness of the instrument in offsetting the risk exposure it is designed to hedge.

As required by the fair value measurements guidance, we have incorporated counterparty credit risk and our credit risk into the fair value measurement of our derivative assets and liabilities, respectively. We derive credit risk from observable data related to credit default swaps. We have not seen a material change in the creditworthiness of those banks acting as derivative counterparties.

The valuation of our interest rate swaps is based on the income approach using a model with inputs that are observable or that can be derived from or corroborated by observable market data. The valuation of our foreign exchange derivatives is based on the market approach using observable market inputs, such as forward rates.

The fair value of our derivative instruments at September 30, 2012 and December 31, 2011 was as follows:

| Designation of Derivatives                        | Balance Sheet Location                    | September 30,<br>2012 | December 31,<br>2011 |
|---|---|-----------------------|----------------------|
| Derivatives designated as hedging instruments     | Other current assets and prepayments:     |                       |                      |
|   | Foreign exchange contracts                | \$369                 | \$780                |
|   | Other assets:                             |                       |                      |
|   | Interest rate swaps                       | 11,643                | 15,465               |
| Derivatives not designated as hedging instruments | Accounts payable and accrued liabilities: |                       |                      |
|   | Foreign exchange contracts                | (240                  | ) (79                |
|   | Other current assets and prepayments:     |                       |                      |
|   | Foreign exchange contracts                | 818                   | 3,450                |
|   | Accounts payable and accrued liabilities: |                       |                      |
|   | Foreign exchange contracts                | (5,194                | ) (1,360             |
|   | Total derivative assets                   | \$12,830              | \$19,695             |
|   | Total derivative liabilities              | (5,434                | ) (1,439             |
|   | Total net derivative assets               | \$7,396               | \$18,256             |



## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## Interest Rate Swaps

Derivatives designated as fair value hedges include interest rate swaps related to fixed rate debt. Changes in the fair value of both the derivative and item being hedged are recognized in earnings. The following represents the results of fair value hedging relationships for the three and nine months ended September 30, 2012 and 2011:

| Derivative Instrument | Location of Gain (Loss) | Three Months Ended September 30,       |         |  |             |
|-----------------------|-------------------------|--|---------|--|-------------|
|                       |                         | Derivative Gain Recognized in Earnings |         | Hedged Item Expense Recognized in Earnings |             |
|                       |                         | 2012                                   | 2011    | 2012                                       | 2011        |
| Interest rate swaps   | Interest expense        | \$1,578                                | \$3,488 | \$(5,484 )                                 | \$(10,109 ) |

  

| Derivative Instrument | Location of Gain (Loss) | Nine Months Ended September 30,        |         |  |             |
|-----------------------|-------------------------|--|---------|--|-------------|
|                       |                         | Derivative Gain Recognized in Earnings |         | Hedged Item Expense Recognized in Earnings |             |
|                       |                         | 2012                                   | 2011    | 2012                                       | 2011        |
| Interest rate swaps   | Interest expense        | \$8,351                                | \$8,406 | \$(25,652 )                                | \$(23,016 ) |

## Foreign Exchange Contracts

We enter into foreign currency exchange contracts to mitigate the currency risk associated with the anticipated purchase of inventory between affiliates and from third parties. These contracts are designated as cash flow hedges. The effective portion of the gain or loss on cash flow hedges is included in accumulated other comprehensive income (AOCI) in the period that the change in fair value occurs and is reclassified to earnings in the period that the hedged item is recorded in earnings. At September 30, 2012 and December 31, 2011, we had outstanding contracts associated with these anticipated transactions with a notional amount of \$21 million and \$19 million, respectively. The net asset value of these contracts was less than \$1 million at September 30, 2012 and December 31, 2011.

The amounts included in AOCI at September 30, 2012 will be recognized in earnings within the next 12 months. No amount of ineffectiveness was recorded in earnings for these designated cash flow hedges.

The following represents the results of cash flow hedging relationships for the three and nine months ended September 30, 2012 and 2011:

| Derivative Instrument      | Three Months Ended September 30,                              |          |   |  |          |
|----------------------------|---|----------|---|--|----------|
|                            | Derivative Gain (Loss) Recognized in AOCI (Effective Portion) |          | Location of Gain (Loss) (Effective Portion) | Gain (Loss) Reclassified from AOCI to Earnings (Effective Portion) |          |
|                            | 2012  | 2011     |   | 2012   | 2011     |
| Foreign exchange contracts | \$ (863 )   | \$ 1,746 | Revenue                                     | \$ 456   | \$(129 ) |
|                            |   |          | Cost of sales                               | (56 )  | (146 )   |
|                            |   |          |   | \$ 400   | \$(275 ) |

  

| Derivative Instrument      | Nine Months Ended September 30,                               |          |   |  |          |
|----------------------------|---|----------|---|--|----------|
|                            | Derivative Gain (Loss) Recognized in AOCI (Effective Portion) |          | Location of Gain (Loss) (Effective Portion) | Gain (Loss) Reclassified from AOCI to Earnings (Effective Portion) |          |
|                            | 2012  | 2011     |   | 2012   | 2011     |
| Foreign exchange contracts | \$ (1,672 )   | \$ 2,049 | Revenue                                     | \$ 1,230   | \$(260 ) |

|               |         |         |   |
|---------------|---------|---------|---|
| Cost of sales | (129    | ) (700  | ) |
|               | \$1,101 | \$ (960 | ) |

We also enter into foreign exchange contracts to minimize the impact of exchange rate fluctuations on short-term intercompany loans and related interest that are denominated in a foreign currency. The revaluation of the intercompany loans and interest and the mark-to-market adjustment on the derivatives are both recorded in earnings. Outstanding foreign exchange contracts to buy or sell various currencies had a net liability value of \$4 million at September 30, 2012 and a net asset value of \$2 million at December 31, 2011. All outstanding contracts at September 30, 2012 mature by the end of the year.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

The following represents the results of our non-designated derivative instruments for the three and nine months ended September 30, 2012 and 2011:

| Derivatives Instrument     | Location of Derivative Gain (Loss)          | Three Months Ended September 30,<br>Derivative Gain (Loss)<br>Recognized in Earnings |         |
|----------------------------|---|--|---------|
|                            |   | 2012   | 2011    |
| Foreign exchange contracts | Selling, general and administrative expense | \$939  | \$2,090 |

  

| Derivatives Instrument     | Location of Derivative Gain (Loss)          | Nine Months Ended September 30,<br>Derivative Gain (Loss)<br>Recognized in Earnings |             |
|----------------------------|---|---|-------------|
|                            |   | 2012  | 2011        |
| Foreign exchange contracts | Selling, general and administrative expense | \$(2,129 )  | \$(18,770 ) |

## Credit-Risk-Related Contingent Features

Certain derivative instruments contain credit-risk-related contingent features that would require us to post collateral based on a combination of our long-term senior unsecured debt ratings and the net fair value of our derivatives. At September 30, 2012, we were not required to post any collateral. The maximum amount of collateral that we would have been required to post at September 30, 2012, had the credit-risk-related contingent features been triggered, was \$5 million.

## Fair Value of Financial Instruments

Our financial instruments include cash and cash equivalents, investment securities, accounts receivable, loan receivables, derivative instruments, accounts payable and debt. The carrying value for cash and cash equivalents, accounts receivable, loans receivable, and accounts payable approximate fair value because of the short maturity of these instruments.

The fair value of our debt is estimated based on recently executed transactions and market price quotations. We classify our debt as Level 2 in the fair value hierarchy. The carrying value and estimated fair value of our debt at September 30, 2012 and December 31, 2011 was as follows:

|                | September 30,<br>2012 | December 31,<br>2011 |
|----------------|-----------------------|----------------------|
| Carrying value | \$3,680,504           | \$4,233,909          |
| Fair value     | \$3,909,732           | \$4,364,176          |

## 10. Restructuring Charges and Asset Impairments

In 2009, we implemented a series of strategic transformation initiatives designed to enhance our responsiveness to changing market conditions, create improved processes and systems to further enable us to invest in future growth and transform and enhance the way we operate as a global company (the 2009 Program). In 2007, we implemented a program to lower our cost structure, accelerate efforts to improve operational efficiencies, and transition our product line to a new generation of fully digital, networked, and remotely-downloadable equipment (the 2007 Program). These programs are substantially complete.

Activity in restructuring reserves for these programs for the nine months ended September 30, 2012 was as follows:

Edgar Filing: PITNEY BOWES INC /DE/ - Form 10-Q

|                               | Severance and<br>benefits costs | Other exit<br>costs | Total     |
|-------------------------------|---------------------------------|---------------------|-----------|
| Balance at January 1, 2012    | \$105,036                       | \$14,075            | \$119,111 |
| Expenses, net                 | 2,608                           | (1,534              | ) 1,074   |
| Cash payments                 | (55,865                         | ) (4,881            | ) (60,746 |
| Balance at September 30, 2012 | \$51,779                        | \$7,660             | \$59,439  |

The majority of the remaining restructuring payments are expected to be paid through 2014; however, due to certain international labor laws and long-term lease agreements, some payments will extend beyond 2014. We expect that cash flows from operations will be sufficient to fund these payments.

PITNEY BOWES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

In connection with our strategic decision to exit the IMS business related to the international delivery of mail and catalogs, asset impairment charges of \$7 million were recorded to write-down the carrying value of certain fixed assets of IMS and \$3 million to write-down the carrying value of certain intangible assets of IMS to their fair values. The fair value of these assets was determined in combination of the written offers received for the IMS business as well as applying an income approach with revised cash flow projections. The inputs used to determine the fair value are classified as Level 3 in the fair value hierarchy. These charges are included in restructuring charges and asset impairments in the Condensed Consolidated Statements of Income. See Note 4 for further details.

#### 11. Commitments and Contingencies

In the ordinary course of business, we are routinely defendants in, or party to a number of pending and threatened legal actions. These may involve litigation by or against us relating to, among other things, contractual rights under vendor, insurance or other contracts; intellectual property or patent rights; equipment, service, payment or other disputes with customers; or disputes with employees. Some of these actions may be brought as a purported class action on behalf of a purported class of employees, customers or others.

In October 2009, the company and certain of its current and former officers were named as defendants in *NECA-IBEW Health & Welfare Fund v. Pitney Bowes Inc. et al.*, a class action lawsuit filed in the U.S. District Court for the District of Connecticut. The complaint asserts claims under the Securities Exchange Act of 1934 on behalf of those who purchased the common stock of the company during the period between July 30, 2007 and October 29, 2007 alleging that the company, in essence, missed two financial projections. Plaintiffs filed an amended complaint in September 2010. After briefing on the motion to dismiss was completed, the plaintiffs filed a new amended complaint on February 17, 2012. We have moved to dismiss this new amended complaint. We expect to prevail in this legal action; however, as litigation is inherently unpredictable, there can be no assurance in this regard. If the plaintiffs do prevail, the results may have a material effect on our financial position, results of operations or cash flows. Based upon our current understanding of the facts and applicable laws, we do not believe there is a reasonable possibility that any loss has been incurred.

#### 12. Segment Information

We conduct our business activities in seven reporting segments within two business groups, Small & Medium Business Solutions and Enterprise Business Solutions. The principal products and services of each of our reporting segments are as follows:

Small & Medium Business Solutions:

North America Mailing: Includes the U.S. and Canadian revenue and related expenses from the sale, rental and financing of our mail finishing, mail creation, shipping equipment and software; supplies; support and other professional services; and payment solutions.

International Mailing: Includes the revenue and related expenses from the sale, rental and financing of our mail finishing, mail creation, shipping equipment and software; supplies; support and other professional services; and payment solutions outside North America.

Enterprise Business Solutions:

Production Mail: Includes the worldwide revenue and related expenses from the sale, support and other professional services of our high-speed, production mail systems, sorting and production print equipment and related software.

Software: Includes the worldwide revenue and related expenses from the sale and support services of non-equipment-based mailing, customer relationship and communication and location intelligence software.

Management Services: Includes worldwide revenue and related expenses from facilities management services; secure mail services; reprographic, document management services; and litigation support and eDiscovery services.

Mail Services: Includes worldwide revenue and related expenses from presort mail services and cross-border mail services.

Marketing Services: Includes revenue and related expenses from direct marketing services for targeted customers. Segment earnings before interest and taxes (EBIT), a non-GAAP measure, is determined by deducting from segment revenue the related costs and expenses attributable to the segment. Segment EBIT excludes interest, taxes, general corporate expenses not allocated to a particular business segment, restructuring charges, asset impairments and goodwill charges which are recognized on a consolidated basis. Management uses segment EBIT to measure profitability and performance at the segment level. Segment

21

---

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

EBIT may not be indicative of our overall consolidated performance and therefore, should be read in conjunction with our consolidated results of operations.

Revenue and EBIT by business segment for the three and nine months ended September 30, 2012 and 2011 was as follows:

|   | Three Months Ended September 30, |             | Nine Months Ended September 30, |             |
|---|----------------------------------|-------------|---------------------------------|-------------|
|   | 2012                             | 2011        | 2012                            | 2011        |
| <b>Revenue:</b>                                       |                                  |             |                                 |             |
| North America Mailing                                 | \$447,920                        | \$475,663   | \$1,362,709                     | \$1,478,355 |
| International Mailing                                 | 154,171                          | 177,797     | 487,665                         | 524,488     |
| Small & Medium Business Solutions                     | 602,091                          | 653,460     | 1,850,374                       | 2,002,843   |
| Production Mail                                       | 122,251                          | 117,220     | 360,334                         | 382,595     |
| Software  | 88,629                           | 109,153     | 288,830                         | 304,921     |
| Management Services                                   | 220,887                          | 235,428     | 679,078                         | 717,513     |
| Mail Services   | 142,182                          | 143,055     | 432,845                         | 421,611     |
| Marketing Services                                    | 39,637                           | 41,408      | 105,690                         | 107,784     |
| Enterprise Business Solutions                         | 613,586                          | 646,264     | 1,866,777                       | 1,934,424   |
| Total revenue   | \$1,215,677                      | \$1,299,724 | \$3,717,151                     | \$3,937,267 |
| <b>EBIT:</b>  |                                  |             |                                 |             |
| North America Mailing                                 | \$168,934                        | \$177,280   | \$514,975                       | \$532,727   |
| International Mailing                                 | 11,286                           | 25,105      | 53,041                          | 75,033      |
| Small & Medium Business Solutions                     | 180,220                          | 202,385     | 568,016                         | 607,760     |
| Production Mail                                       | 3,555                            | (3,426)     | 11,928                          | 12,971      |
| Software  | 956                              | 16,564      | 20,135                          | 31,618      |
| Management Services                                   | 10,266                           | 18,248      | 36,187                          | 59,256      |
| Mail Services   | 16,671                           | 35,107      | 75,661                          | 55,191      |
| Marketing Services                                    | 9,297                            | 8,716       | 21,617                          | 19,668      |
| Enterprise Business Solutions                         | 40,745                           | 75,209      | 165,528                         | 178,704     |
| Total EBIT  | 220,965                          | 277,594     | 733,544                         | 786,464     |
| <b>Reconciling items:</b>                             |                                  |             |                                 |             |
| Interest, net (1)                                     | (45,088)                         | (49,097)    | (142,853)                       | (148,219)   |
| Corporate and other expenses                          | (39,960)                         | (50,046)    | (138,521)                       | (135,426)   |
| Restructuring charges and asset impairments           | (9,986)                          | (32,956)    | (11,060)                        | (63,974)    |
| Goodwill impairment                                   | (18,315)                         | (45,650)    | (18,315)                        | (45,650)    |
| Income from continuing operations before income taxes | \$107,616                        | \$99,845    | \$422,795                       | \$393,195   |

(1) Includes financing interest expense, other interest expense and interest income.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 13. Pensions and Other Benefit Programs

## Defined Benefit Pension Plans

The components of net periodic benefit cost for defined benefit pension plans for the three and nine months ended September 30, 2012 and 2011 were as follows:

|                                    | Three Months Ended September 30, |           |           |           |
|------------------------------------|----------------------------------|-----------|-----------|-----------|
|                                    | United States                    |           | Foreign   |           |
|                                    | 2012                             | 2011      | 2012      | 2011      |
| Service cost                       | \$4,735                          | \$4,862   | \$1,774   | \$1,836   |
| Interest cost                      | 20,260                           | 21,935    | 6,909     | 7,089     |
| Expected return on plan assets     | (30,406                          | ) (30,765 | ) (8,069  | ) (7,945  |
| Amortization of transition credit  | —                                | —         | (2        | ) (2      |
| Amortization of prior service cost | 200                              | 36        | 28        | 42        |
| Recognized net actuarial loss      | 13,240                           | 9,381     | 3,558     | 2,782     |
| Settlement                         | —                                | —         | 192       | —         |
| Special termination benefits       | —                                | 229       | —         | —         |
| Curtailement                       | —                                | 435       | —         | —         |
| Net periodic benefit cost          | \$8,029                          | \$6,113   | \$4,390   | \$3,802   |
|                                    |                                  |           |           |           |
|                                    | Nine Months Ended September 30,  |           |           |           |
|                                    | United States                    |           | Foreign   |           |
|                                    | 2012                             | 2011      | 2012      | 2011      |
| Service cost                       | \$14,204                         | \$14,587  | \$5,805   | \$5,650   |
| Interest cost                      | 60,780                           | 65,805    | 20,766    | 21,344    |
| Expected return on plan assets     | (91,218                          | ) (92,294 | ) (24,133 | ) (23,978 |
| Amortization of transition credit  | —                                | —         | (6        | ) (6      |
| Amortization of prior service cost | 602                              | 109       | 83        | 130       |
| Recognized net actuarial loss      | 39,719                           | 28,142    | 10,546    | 8,307     |
| Settlement                         | —                                | —         | 442       | —         |
| Special termination benefits       | —                                | 989       | —         | 10        |
| Curtailement                       | —                                | 2,531     | —         | 224       |
| Net periodic benefit cost          | \$24,087                         | \$19,869  | \$13,503  | \$11,681  |

Through September 30, 2012, we contributed \$92 million to our U.S. pension plan and \$29 million to our foreign pension plans. This includes special contributions of \$85 million to our U.S. pension plan and \$10 million to our foreign pension plans.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## Nonpension Postretirement Benefit Plans

The components of net periodic benefit cost for nonpension postretirement benefit plans for the three and nine months ended September 30, 2012 and 2011 were as follows:

|                                      | Three Months Ended |         | Nine Months Ended September |          |
|--------------------------------------|--------------------|---------|-----------------------------|----------|
|                                      | September 30,      |         | 30,                         |          |
|                                      | 2012               | 2011    | 2012                        | 2011     |
| Service cost                         | \$801              | \$834   | \$2,560                     | \$2,501  |
| Interest cost                        | 2,896              | 3,387   | 8,685                       | 10,158   |
| Amortization of prior service credit | (523               | ) (626  | ) (1,569                    | ) (1,878 |
| Amortization of net loss             | 2,054              | 1,917   | 6,111                       | 5,750    |
| Special termination benefits         | —                  | 44      | —                           | 157      |
| Curtailment                          | —                  | 416     | —                           | 1,652    |
| Net periodic benefit cost            | \$5,228            | \$5,972 | \$15,787                    | \$18,340 |

Contributions for benefit payments were \$7 million and \$9 million for the three months ended September 30, 2012 and 2011, respectively, and \$21 million and \$23 million for the nine months ended September 30, 2012 and 2011, respectively.

## 14. Discontinued Operations

During the nine months ended September 30, 2012, we recognized \$19 million of tax benefits in discontinued operations arising from the resolution of tax examinations related to our Capital Services business that was sold in 2006. During the third quarter of 2011, we entered into a series of settlements with the IRS in connection with their examination of our tax years 2001-2004. We agreed upon the tax treatment of a number of disputed issues, including issues related to our Capital Services business, and as a result, \$60 million of previously provided tax and interest reserves were released through discontinued operations.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 15. Earnings per Share

The calculations of basic and diluted earnings per share for the three and nine months ended September 30, 2012 and 2011 are presented below. The sum of earnings per share amounts may not equal the totals due to rounding.

|  | Three Months Ended<br>September 30, |           | Nine Months Ended<br>September 30, |           |
|--|-------------------------------------|-----------|------------------------------------|-----------|
|  | 2012                                | 2011      | 2012                               | 2011      |
| Numerator:   |                                     |           |                                    |           |
| Amounts attributable to common stockholders:   |                                     |           |                                    |           |
| Income from continuing operations  | \$76,533                            | \$112,339 | \$315,494                          | \$302,095 |
| Income from discontinued operations  | —                                   | 60,428    | 19,332                             | 57,911    |
| Net income (numerator for diluted EPS)   | 76,533                              | 172,767   | 334,826                            | 360,006   |
| Less: Preference stock dividend  | (12                                 | ) (15     | ) (38                              | ) (44     |
| Income attributable to common stockholders (numerator for basic EPS)                         | \$76,521                            | \$172,752 | \$334,788                          | \$359,962 |
| Denominator (in thousands):  |                                     |           |                                    |           |
| Weighted-average shares used in basic EPS  | 200,593                             | 201,294   | 200,266                            | 202,664   |
| Effect of dilutive shares:   |                                     |           |                                    |           |
| Preferred stock  | 2                                   | 2         | 2                                  | 2         |
| Preference stock   | 399                                 | 447       | 399                                | 451       |
| Stock plans  | 608                                 | 451       | 458                                | 366       |
| Weighted-average shares used in diluted EPS  | 201,602                             | 202,194   | 201,125                            | 203,483   |
| Basic earnings per share:  |                                     |           |                                    |           |
| Income from continuing operations  | \$0.38                              | \$0.56    | \$1.58                             | \$1.49    |
| Income from discontinued operations  | —                                   | 0.30      | 0.10                               | 0.29      |
| Net income   | \$0.38                              | \$0.86    | \$1.67                             | \$1.78    |
| Diluted earnings per share:  |                                     |           |                                    |           |
| Income from continuing operations  | \$0.38                              | \$0.56    | \$1.57                             | \$1.48    |
| Income from discontinued operations  | —                                   | 0.30      | 0.10                               | 0.28      |
| Net income   | \$0.38                              | \$0.85    | \$1.66                             | \$1.77    |
| Anti-dilutive shares not used in calculating diluted weighted-average shares (in thousands): | 13,607                              | 15,442    | 14,391                             | 15,435    |

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations  
Forward-Looking Statements

This Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) contains statements that are forward-looking. We want to caution readers that any forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 in this Form 10-Q may change based on various factors. These forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties and actual results could differ materially. Words such as "estimate", "target", "project", "plan", "believe", "expect", "anticipate", "intend", and similar expressions may identify such forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Factors which could cause future financial performance to differ materially from the expectations as expressed in any forward-looking statement made by or on our behalf include, without limitation:

- declining physical mail volumes
- mailers' utilization of alternative means of communication or competitors' products
- access to capital at a reasonable cost to continue to fund various discretionary priorities, including business investments, pension contributions and dividend payments
- timely development and acceptance of new products and services
- successful entry into new markets
- success in gaining product approval in new markets where regulatory approval is required
- changes in postal or banking regulations
- interrupted use of key information systems
- third-party suppliers' ability to provide product components, assemblies or inventories
- our success at managing the relationships with our outsource providers, including the costs of outsourcing functions and operations not central to our business
- changes in privacy laws
- intellectual property infringement claims
- regulatory approvals and satisfaction of other conditions to consummate and integrate any acquisitions
- negative developments in economic conditions, including adverse impacts on customer demand
- our success at managing customer credit risk
- significant changes in pension, health care and retiree medical costs
- changes in interest rates, foreign currency fluctuations or credit ratings
- income tax adjustments or other regulatory levies for prior audit years and changes in tax laws, rulings or regulations
- impact on mail volume resulting from concerns over the use of the mail for transmitting harmful biological agents
- changes in international or national political conditions, including any terrorist attacks
- acts of nature

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our Condensed Consolidated Financial Statements contained in this report and our Annual Report to Stockholders on Form 10-K for the year ended December 31, 2011 (2011 Annual Report). All table amounts are presented in millions of dollars, unless otherwise stated. Table amounts may not sum to the total due to rounding.

Overview

For the third quarter of 2012, revenue decreased 6% to \$1,216 million compared to \$1,300 million in the prior year quarter. Software revenue declined 17% due in part to a strong prior year third quarter and an overall slowdown in our global markets, particularly in the public sector. Financing revenue declined 9% due to the impact of lower equipment sales in prior periods. Rental revenue and supplies revenue declined 8% and 10% respectively, due to a decrease in mail volumes and our installed meter base, and in the case of supplies, also due to lower ink and toner sales. Business services revenue declined 5% due to Management Services account contractions and pricing pressure and equipment

sales declined 4% due uncertain economic conditions and revenue from a postal rate change in France in the prior year that did not recur this year. Foreign currency translation had an unfavorable impact of 1% on revenue in the quarter.

The results for the quarter also include goodwill and asset impairment charges totaling \$28 million in connection with a strategic decision to exit the International Mail Services (IMS) business related to the international delivery of mail and catalogs. The total impairment charge consists of a goodwill impairment charge of \$18 million and asset impairment charges of \$10 million. Net income from continuing operations attributable to common stockholders was \$77 million, or \$0.38 per diluted share for the quarter compared to \$112 million or \$0.56 per diluted share for the prior year quarter.

For the nine months ended September 30, 2012, revenue decreased 6% to \$3,717 million compared to \$3,937 million for the nine months ended September 30, 2011. Our overall revenue continues to be adversely impacted by worldwide economic conditions, declining mail volumes, Management Services account contractions and pricing pressures. Foreign currency translation had an unfavorable impact of

1% on revenue. Net income from continuing operations attributable to common stockholders was \$315 million, or \$1.57 per diluted share for the nine months ended September 30, 2012 compared to \$302 million, or \$1.48 per diluted share for the nine months ended September 30, 2011.

Through September 30, 2012, we generated \$440 million of cash from operations and received \$106 million from the sale of leveraged lease assets. We used cash to redeem \$550 million of long-term debt, pay dividends of \$234 million and fund capital investments of \$128 million.

#### Outlook

Worldwide economic weakness continues to create a challenging business environment causing many of our customers to remain cautious about spending and, therefore, impacting the performance of our business segments. Small and Medium Business Solutions (SMB) revenues will continue to be challenged by the decline in physical mail volumes as alternative means of communications evolve and gain further acceptance. The rate of decline in equipment sales slowed in the third quarter, due in part to global sales of our Connect+™ communications systems, SendSuite Live™ shipping solutions and pbWebConnect™ mailing systems. We anticipate that the historical equipment sales trends should show improvement in future periods. A slowing of the rate of decline for overall SMB revenue will lag that of equipment sales because recurring revenue streams follow the equipment sales.

We anticipate revenue growth in certain of our Enterprise Business Solutions segments from continued expansion in Mail Services' presort operations, new ecommerce initiatives and market acceptance for our new solutions that help customers grow their business by more effectively managing their physical and digital communications with their customers. We recently announced a partnership with Ebay to provide ecommerce solutions for international package delivery which will commence in the fourth quarter in time for the holiday season. We will continue to focus on the growth potential of ecommerce products and solutions; and in line with this strategy, we recently decided to exit the IMS business related to the international delivery of mail and catalogs.

Our growth strategies will focus on leveraging our expertise in physical communications with our expanding capabilities in digital and hybrid communications. We will continue to develop and invest in products, software, services and solutions that help customers grow their business by more effectively communicating with their customers across physical, digital and hybrid channels. We expect our mix of business will continue to shift to more enterprise related products and solutions, and that these new revenue streams will have lower margins than our traditional Mailing business. We intend to further streamline our business operations and reduce our cost structure to address this margin mix. We expect that these actions will result in a pretax restructuring charge in the fourth quarter of \$40 million to \$60 million.

## RESULTS OF OPERATIONS

Revenue by source and the related cost of revenue are shown in the following tables:

## Revenue

|                   | Three Months Ended September 30, |         |          | Nine Months Ended September 30, |         |          |
|-------------------|----------------------------------|---------|----------|---------------------------------|---------|----------|
|                   | 2012                             | 2011    | % change | 2012                            | 2011    | % change |
| Equipment sales   | \$212                            | \$221   | (4)%     | \$657                           | \$706   | (7)%     |
| Supplies          | 67                               | 74      | (10)%    | 214                             | 236     | (9)%     |
| Software          | 93                               | 113     | (17)%    | 302                             | 318     | (5)%     |
| Rentals           | 142                              | 154     | (8)%     | 428                             | 467     | (8)%     |
| Financing         | 124                              | 136     | (9)%     | 374                             | 413     | (10)%    |
| Support services  | 172                              | 175     | (2)%     | 516                             | 531     | (3)%     |
| Business services | 405                              | 425     | (5)%     | 1,226                           | 1,266   | (3)%     |
| Total revenue     | \$1,216                          | \$1,300 | (6)%     | \$3,717                         | \$3,937 | (6)%     |

## Cost of revenue

|                            | Three Months Ended September 30, |       |                       |       | Nine Months Ended September 30, |         |                       |       |
|----------------------------|----------------------------------|-------|-----------------------|-------|---------------------------------|---------|-----------------------|-------|
|                            |                                  |       | Percentage of Revenue |       |                                 |         | Percentage of Revenue |       |
|                            | 2012                             | 2011  | 2012                  | 2011  | 2012                            | 2011    | 2012                  | 2011  |
| Cost of equipment sales    | \$106                            | \$98  | 49.8%                 | 44.0% | \$309                           | \$317   | 47.1%                 | 44.9% |
| Cost of supplies           | 21                               | 23    | 30.9%                 | 30.4% | 65                              | 74      | 30.6%                 | 31.5% |
| Cost of software           | 23                               | 23    | 24.4%                 | 20.7% | 68                              | 74      | 22.6%                 | 23.1% |
| Cost of rentals            | 25                               | 36    | 17.7%                 | 23.2% | 87                              | 108     | 20.4%                 | 23.1% |
| Financing interest expense | 20                               | 21    | 15.8%                 | 15.8% | 61                              | 67      | 16.4%                 | 16.2% |
| Cost of support services   | 107                              | 114   | 62.4%                 | 65.1% | 334                             | 345     | 64.7%                 | 65.0% |
| Cost of business services  | 316                              | 326   | 77.9%                 | 76.8% | 948                             | 985     | 77.3%                 | 77.8% |
| Total cost of revenue      | \$617                            | \$641 | 50.7%                 | 49.3% | \$1,874                         | \$1,969 | 50.4%                 | 50.0% |

## Equipment sales

Equipment sales revenue decreased 4% to \$212 million in the quarter compared to the prior year quarter. Foreign currency translation had an unfavorable impact on revenue of 2% and equipment sales for the prior year quarter included \$6 million for scale updates from a postal rate change in France which did not recur this year. Excluding the effects of foreign currency translation and the revenue from the postal rate change, equipment sales for the quarter were slightly higher than the prior year quarter as higher sales of our high-end production mail and print equipment offset lower equipment sales in our mailing businesses. For the year-to-date period, equipment sales revenue decreased 7% to \$657 million compared to the prior year period, primarily due to worldwide economic conditions causing customers to postpone purchases of new equipment. Foreign currency translation had an unfavorable impact on revenue of 2% on the year-to-date period. Cost of equipment sales as a percentage of revenue increased to 49.8% in the quarter compared to 44.0% in the prior year quarter due to fewer lease extensions compared to the prior year period and the margin from the postal rate change revenue. For the year-to-date period, cost of equipment sales as a percentage of revenue increased to 47.1% compared to 44.9% in the prior year, primarily due to a higher mix of lower margin product sales and pricing pressure on competitive placements.

## Supplies

Supplies revenue decreased 10% to \$67 million and 9% to \$214 million in the quarter and year-to-date periods, respectively, compared with the same periods in 2011, primarily due to reduced mail volumes, fewer installed meters worldwide and lower ink and toner sales. Foreign currency translation had an unfavorable impact on revenue of 3% in the quarter and 2% in the year-to-date period. Cost of supplies as a percentage of revenue was 30.9% in the quarter

compared with 30.4% in the prior year quarter. For the year-to-date period, the cost of supplies as a percentage of revenue improved to 30.6% compared to 31.5% in the comparable prior year period primarily due to a favorable mix of higher margin core supplies sales and price increases during the first half of 2012.

Software

Software revenue decreased 17% to \$93 million in the quarter and 5% to \$302 million in the year-to-date period compared with the same periods in 2011. The decrease in the quarter was primarily due to a strong prior year third quarter and a decline in the volume of business

and contract values, particularly in North America and the Asia-Pacific region. The year-to-date decrease was attributable to the decline in the volume of business and contract values in the third quarter and weak European sales driven by weak economic conditions and constrained public sector spending. Foreign currency had an unfavorable impact on revenue of 1% in the quarter and year-to-date periods. Cost of software as a percentage of revenue increased to 24.4% in the quarter compared with 20.7% in the prior year quarter primarily due to the decline in revenue. On a year-to-date basis, cost of software as a percentage of revenue improved slightly to 22.6% compared with 23.1% in the prior year-to-date period.

#### Rentals

Rentals revenue decreased 8% in both the quarter and year-to-date periods to \$142 million and \$428 million, respectively, compared with the same periods in 2011, primarily due to declines in North America from lower mail volumes and fewer meters in service and a change in mix from rental to equipment sales in France. Foreign currency translation had an unfavorable impact on revenue of 2% in the quarter and 1% in the year-to-date period. Cost of rentals as a percentage of revenue improved to 17.7% in the quarter compared to 23.2% in the prior year quarter and to 20.4% for the year-to-date period compared with 23.1% in the prior year-to-date period mainly due to lower depreciation expense.

#### Financing

Financing revenue decreased 9% to \$124 million in the quarter and 10% to \$374 million in the year-to-date period compared with the same periods in 2011, primarily due to lower equipment sales in prior periods. Financing interest expense as a percentage of revenue was 15.8% in both the current year and prior year quarter and 16.4% and 16.2% in the current and prior year-to-date periods, respectively. In computing our financing interest expense, which represents our cost of borrowing associated with the generation of financing revenue, we assume a 10:1 leveraging ratio of debt to equity and apply our overall effective interest rate to the average outstanding finance receivables.

#### Support Services

Support services revenue decreased 2% in the quarter to \$172 million and 3% in the year-to-date period to \$516 million compared with the same periods in 2011. The decreases were primarily driven by the unfavorable impacts of foreign currency translation, which reduced revenue by 2% in both the quarter and year-to-date periods. Cost of support services as a percentage of revenue improved to 62.4% in the quarter compared with 65.1% in the prior year quarter due to improving margins in our International Mailing business. Cost of support services as a percentage of revenue in the year-to-date period was 64.7% compared to 65.0% in the prior year-to-date period.

#### Business Services

Business services revenue decreased 5% to \$405 million and 3% to \$1,226 million in the quarter and year-to-date period, respectively, compared with the same periods in 2011. The decrease is primarily due to lower volumes, account contractions and pricing pressures on new business and contract renewals in our Management Services business. Foreign currency translation had an unfavorable impact of 1% on both the quarter and year-to-date revenue. Cost of business services as a percentage of revenue increased to 77.9% in the quarter compared with 76.8% in the prior year quarter primarily due to margin compression in our Management Services business. Cost of business services as a percentage of revenue was 77.3% in the year-to-date period compared to 77.8% in the prior year year-to-date period.

#### Selling, general and administrative (SG&A)

SG&A expense decreased 6% in both the quarter and year-to-date periods to \$401 million and \$1,204 million, respectively, compared to the same periods in the prior year. The quarter and year-to-date decreases were primarily driven by a 4% decrease in employee-related costs due to prior restructuring actions and productivity initiatives, a 2% decrease in depreciation and amortization expense due to lower capital expenditures and asset impairment charges in prior periods and a 2% decrease in credit loss and bad debt provisions.

#### Restructuring charges and asset impairments

#### Goodwill impairment

We perform our annual goodwill impairment test during the fourth quarter of each year, or sooner, if circumstances indicate an impairment may exist. Based on the recent performance of our IMS business and to enable us to better

focus on higher growth cross-border ecommerce parcel opportunities, in the third quarter 2012, we began exploring strategic alternatives for the IMS business. In October 2012, we made a strategic decision to exit the IMS business related to the international delivery of mail and catalogs. We are engaged in negotiations with potential buyers and have received preliminary indications of interest and written offers. As a result of these factors, we concluded that it was more likely than not that the fair value of the IMS reporting unit was below its book value and an interim impairment test was performed. The fair value of the reporting unit was determined in combination of the written offers received as well as applying an income approach with revised cash flow projections. Based on the results of our impairment test, a non-cash goodwill impairment charge of \$18 million was recorded in the third quarter 2012 to write-down the carrying value of goodwill associated with the IMS business to its implied fair value. We also recorded impairment charges of \$10 million to write-down the carrying values of certain intangible and fixed assets associated with the IMS business to their respective fair values. These asset impairment charges are recorded as restructuring charges and asset impairments in the Condensed Consolidated Statements of Income.

In the third quarter of 2011, in connection with our long-term planning and budgeting process and due to the continuing under-performance of the IMS operations, a goodwill impairment charge of \$46 million was recorded and asset impairment charges of \$12 million were recorded to write-down goodwill and certain tangible and intangible assets of IMS to their implied fair values. Restructuring charges and asset impairments for the three and nine months ended September 30, 2011 also include \$21 million and \$52 million, respectively, related to restructuring actions.

Other (income) expense, net

Other (income) expense, net is comprised of the following:

|  | (Income) / Expense |         |
|--|--------------------|---------|
|  | 2012               | 2011    |
| Insurance proceeds                                   | \$(11 )            | \$(18 ) |
| Loss on forward starting swap agreement              | 6                  | —       |
| Early termination of debt                            | 2                  | —       |
| Pretax loss on sale of certain leverage lease assets | 4                  | 7       |
| Other (income) expense, net                          | \$1                | \$(11 ) |

Insurance proceeds relate to proceeds received in connection with the 2011 fire at our Dallas presort facility.

During the year, we entered into forward starting swap agreements with an aggregate notional value of \$150 million to hedge interest rate risk associated with a forecasted issuance of long-term debt. The anticipated debt issuance did not occur prior to the expiration of these swap agreements and a loss of \$6 million was recognized.

On June 30, 2012, we redeemed our \$400 million, 4.625% notes (the 2012 Notes) that were due in October 2012. As a result of the early redemption of the 2012 Notes, we incurred a net loss of \$2 million comprised of a loss of \$4 million for a make-whole payment and a gain of \$2 million from the termination of interest rate swap contracts.

In the first quarter of 2012 and third quarter of 2011, we sold certain non-U.S. leveraged lease assets. The 2012 sale resulted in a pretax loss of \$4 million and a tax benefit of \$17 million (net after-tax gain \$13 million) and the 2011 sale resulted in a pretax loss of \$7 million and a tax benefit of \$34 million (net after-tax gain \$27 million). The tax benefit is included in the provision for income taxes.

Income taxes

See Note 7 to the unaudited Condensed Consolidated Financial Statements.

Discontinued operations

See Note 14 to the unaudited Condensed Consolidated Financial Statements.

Preferred stock dividends of subsidiaries attributable to noncontrolling interests

See Note 6 to the unaudited Condensed Consolidated Financial Statements.

## Business segment results

We conduct our business activities in seven reporting segments within two business groups, Small & Medium Business Solutions and Enterprise Business Solutions. The following tables show revenue and EBIT by business segment for the three and nine months ended September 30, 2012 and 2011. Segment EBIT, a non-GAAP measure, is determined by deducting from segment revenue the related costs and expenses attributable to the segment. Segment EBIT excludes interest, taxes, general corporate expenses not allocated to a particular business segment, restructuring charges, asset impairments and goodwill charges, which are recognized on a consolidated basis. Management uses segment EBIT to measure profitability and performance at the segment level. Segment EBIT may not be indicative of our overall consolidated performance and therefore, should be read in conjunction with our consolidated results of operations. Refer to Note 12 to the Condensed Consolidated Financial Statements for a reconciliation of segment EBIT to income from continuing operations before income taxes.

| Revenue                           | Three Months Ended September 30, |         |          | Nine Months Ended September 30, |         |          |
|-----------------------------------|----------------------------------|---------|----------|---------------------------------|---------|----------|
|                                   | 2012                             | 2011    | % change | 2012                            | 2011    | % change |
| North America Mailing             | \$448                            | \$476   | (6)%     | \$1,363                         | \$1,478 | (8)%     |
| International Mailing             | 154                              | 178     | (13)%    | 488                             | 524     | (7)%     |
| Small & Medium Business Solutions | 602                              | 654     | (8)%     | 1,850                           | 2,003   | (8)%     |
| Production Mail                   | 122                              | 117     | 4%       | 360                             | 383     | (6)%     |
| Software                          | 89                               | 109     | (19)%    | 289                             | 305     | (5)%     |
| Management Services               | 221                              | 235     | (6)%     | 679                             | 718     | (5)%     |
| Mail Services                     | 142                              | 143     | (1)%     | 433                             | 422     | 3%       |
| Marketing Services                | 40                               | 41      | (4)%     | 106                             | 108     | (2)%     |
| Enterprise Business Solutions     | 614                              | 646     | (5)%     | 1,867                           | 1,934   | (3)%     |
| Total                             | \$1,216                          | \$1,300 | (6)%     | \$3,717                         | \$3,937 | (6)%     |
| EBIT                              | Three Months Ended September 30, |         |          | Nine Months Ended September 30, |         |          |
|                                   | 2012                             | 2011    | % change | 2012                            | 2011    | % change |
| North America Mailing             | \$169                            | \$177   | (5)%     | \$515                           | \$533   | (3)%     |
| International Mailing             | 11                               | 25      | (55)%    | 53                              | 75      | (29)%    |
| Small & Medium Business Solutions | 180                              | 202     | (11)%    | 568                             | 608     | (7)%     |
| Production Mail                   | 4                                | (3)     | 204%     | 12                              | 13      | (8)%     |
| Software                          | 1                                | 17      | (94)%    | 20                              | 32      | (36)%    |
| Management Services               | 10                               | 18      | (44)%    | 36                              | 59      | (39)%    |
| Mail Services                     | 17                               | 35      | (53)%    | 76                              | 55      | 37%      |
| Marketing Services                | 9                                | 9       | 7%       | 22                              | 20      | 10%      |
| Enterprise Business Solutions     | 41                               | 75      | (46)%    | 166                             | 179     | (7)%     |
| Total                             | \$221                            | \$278   | (20)%    | \$734                           | \$786   | (7)%     |

## Small &amp; Medium Business Solutions

Small & Medium Business Solutions revenue decreased 8% in the quarter and year-to-date periods to \$602 million and \$1,850 million, respectively, compared to the same periods in 2011. EBIT decreased 11% to \$180 million and 7% to \$568 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2011.

Within the Small & Medium Business Solutions group:

## North America Mailing

Revenue for the North America Mailing segment decreased 6% to \$448 million and 8% to \$1,363 million in the quarter and year-to-date periods, respectively, compared with the same periods in 2011. Compared to the prior year periods, equipment sales declined 4% in the quarter and 6% in the year-to-date period due to continued concerns about economic conditions and declining mail volumes. Financing revenue declined 7% in the quarter and 9% in the year-to-date period compared to the prior year periods due to declining equipment sales in prior periods. Rentals

revenue declined 6% in the quarter and 8% in the year-to-date period as compared to the prior year periods primarily due to fewer meters in service and supplies revenue declined 12% in the quarter and 13% in the year-to-date period as compared to the prior year periods due to lower mail volumes, a declining installed meter base and lower ink and toner sales.

EBIT decreased 5% to \$169 million and 3% to \$515 million in the quarter and year-to-date periods, respectively, compared with the same periods in 2011 primarily due to the decline in revenue.

#### International Mailing

Revenue for the International Mailing segment decreased 13% to \$154 million and 7% to \$488 million in the quarter and year-to-date periods, respectively, compared with the same periods in 2011; however, foreign currency translation had an unfavorable impact on revenue of 6% in both the quarter and year-to-date periods. The underlying decrease in the quarter was primarily due to lower equipment sales due to the prior year revenue of \$6 million from the postal rate change in France and the uncertain economic environment in Europe.

The underlying decrease in the year-to-date revenue was driven by a 5% decline in rentals revenue due a change in mix from rentals to equipment sales in France and a 4% decrease in financing revenue, partially offset by higher equipment sales in France and the Nordics.

EBIT decreased 55% to \$11 million and 29% to \$53 million in the quarter and year-to-date periods, respectively, compared with the same periods in 2011, primarily due to an increase in the mix of lower margin product sales, the margin from the postal rate change revenue recognized in the prior year and foreign currency translation.

#### Enterprise Business Solutions

Enterprise Business Solutions revenue for the quarter and year-to-date periods decreased 5% to \$614 million and 3% to \$1,867 million, respectively, compared to the same periods in 2011. EBIT decreased 46% to \$41 million in the quarter and 7% to \$166 million in the year-to-date period compared with the same periods in 2011; however, these results were impacted by the fire in 2011 that destroyed a presort facility located in Dallas. See Mail Services section below. Within the Enterprise Business Solutions group:

#### Production Mail

Revenue for the Production Mail segment increased 4% to \$122 million in the quarter compared to the prior year quarter, driven primarily by an increase in international equipment sales due in part to a weak prior year third quarter and the positive results of a trade show during the second quarter. Despite the increase in the third quarter, year-to-date revenues of \$360 million were down 6% compared to the prior year due to uncertain economic conditions, resulting in customers worldwide prolonging their capital investment decisions and opting to retain their existing equipment longer than usual. Foreign currency translation had an unfavorable impact on revenue of 3% in both the quarter and year-to-date periods.

EBIT was \$4 million in the quarter compared to a loss of \$3 million in the prior year quarter primarily due to the increase in revenue and lower operating expenses. For the year-to-date period, EBIT decreased 8% to \$12 million compared with the prior year period primarily due to the decline in revenue partially offset by lower operating expenses.

#### Software

Revenue for the Software segment decreased 19% to \$89 million and 5% to \$289 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2011. The decrease in the quarter was due to a strong prior year third quarter and an overall slowdown in our global markets, particularly in North America and the Asia-Pacific region. The decrease in the year-to-date period was driven by the slowdown in our global markets due to uncertain economic conditions and constrained public sector spending.

EBIT decreased 94% to \$1 million and 36% to \$20 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2011, primarily due to the decline in revenue and higher research and development and marketing costs.

#### Management Services

Revenue for the Management Services segment decreased 6% to \$221 million and 5% to \$679 million, in the quarter and year-to-date periods, respectively, compared with the same periods in 2011. EBIT decreased 44% to \$10 million

and 39% to \$36 million, in the quarter and year-to-date periods, respectively, compared with the same periods in 2011. The decline in revenue and EBIT was primarily due to lower volumes, account contractions and pricing pressure. Foreign currency translation had an unfavorable impact on revenue of 1% in both the quarter and year-to-date periods.

#### Mail Services

Revenue for the Mail Services segment decreased 1% to \$142 million in the quarter due to lower volumes in our International Mail Services business partially offset by higher standard mail volumes in our Presort business. For the year-to-date period, revenue increased 3% to \$433 million compared to the prior year period; however, prior year revenue was adversely impacted by \$19 million due to the fire that destroyed our Dallas presort facility. Excluding the impact of the fire, year-to-date revenue decreased 2% compared to the prior year due to lower volumes in our International Mail Services business partially offset by higher standard mail volumes in our Presort business.

EBIT for the quarter decreased 53% to \$17 million compared to the prior year; however, EBIT for the prior year quarter includes an \$18 million benefit from fire-related insurance recoveries. Excluding this benefit, EBIT decreased 3% primarily due to investments in our ecommerce business. For the year-to-date period, EBIT increased 37% to \$76 million, compared to the prior year period. However, current year EBIT includes a benefit of \$11 million from fire-related insurance recoveries while prior year EBIT includes the \$19 million

adverse impact on revenue and the \$18 million benefit from insurance recoveries. Excluding these fire-related impacts, EBIT increased 14% due to growth in our Presort business.

#### Marketing Services

Revenue for the Marketing Services segment for the quarter and year-to-date periods was \$40 million and \$106 million, respectively, down slightly when compared to the same periods in 2011 primarily due to a decline in household moves. EBIT for the quarter and year-to-date periods improved slightly to \$9 million and \$22 million, respectively, when compared with the same periods in 2011 due to lower print production costs and administrative costs.

#### LIQUIDITY AND CAPITAL RESOURCES

We believe that cash flow from operations, existing cash and investments, as well as borrowing capacity under our commercial paper program should be sufficient to support our business operations, interest and dividend payments, share repurchases, debt maturities, capital expenditures, and to cover customer deposits. We have the ability to supplement short-term liquidity and fund the long-term needs of our business through broad access to capital markets, a credit line facility, and our effective shelf registration statement. Cash and cash equivalents and short-term investments were \$461 million at September 30, 2012 and \$869 million at December 31, 2011.

Cash and cash equivalents held by our foreign subsidiaries are generally used to support the liquidity needs of these subsidiaries. Cash and cash equivalents held by our foreign subsidiaries were \$143 million at September 30, 2012 and \$538 million at December 31, 2011. Most of these amounts could be repatriated to the United States but would be subject to additional taxes. Repatriation of some foreign balances is restricted by local laws. With the exception of the impact of unusual sales of leveraged lease assets and the one-time restructuring of our Canadian operations that led us to accrue taxes for the repatriation of certain earnings, it is our intention to permanently reinvest substantially all of our foreign cash in our foreign operations.

There has not been a material variation in the underlying sources of cash flows currently used to finance our operations, and we have had consistent access to the commercial paper market. During the second quarter, one of the rating agencies reduced our credit ratings. There can be no assurances that one or more of the rating agencies will not take additional adverse actions in the future.

We continuously review our liquidity profile through published credit ratings and the credit default swap market. We monitor the creditworthiness of those banks acting as derivative counterparties, depository banks or credit providers.

#### Cash Flow Summary

The change in cash and cash equivalents is as follows:

|  | Nine Months Ended September 30, |       |         |
|--|---------------------------------|-------|---------|
|  | 2012                            | 2011  | Change  |
| Net cash provided by operating activities                    | \$440                           | \$750 | \$(310) |
| Net cash used in investing activities                        | (96)                            | (140) | 44      |
| Net cash used in financing activities                        | (777)                           | (374) | (403)   |
| Effect of exchange rate changes on cash and cash equivalents | 2                               | (5)   | 7       |
| (Decrease) increase in cash and cash equivalents             | \$(431)                         | \$231 | \$(662) |

Net cash provided by operating activities was \$440 million for the nine months ended September 30, 2012 compared to \$750 million for the nine months ended September 30, 2011. The decrease of \$310 million was primarily due to higher tax payments in 2012, as a result of tax payments related to the sale of leveraged lease assets, the loss of bonus depreciation and higher income tax refunds received in 2011, and lower collections of finance and accounts receivables in 2012.

Net cash used in investing activities was \$96 million for the nine months ended September 30, 2012 compared to \$140 million for the nine months ended September 30, 2011. The decrease in cash used in investing activities was primarily due to reduced investments in short-term and other investments.

Net cash used in financing activities was \$777 million for the nine months ended September 30, 2012 compared to \$374 million for the nine months ended September 30, 2011. This increase in cash used in financing activities was due to the repayment of \$550 million of long-term debt during 2012 compared to the repayment of \$50 million of commercial paper borrowings during 2011. There were no share repurchases during 2012 compared to \$100 million of share repurchases in 2011.

## Financings and Capitalization

We are a Well-Known Seasoned Issuer with the Securities and Exchange Commission, which allows us to issue debt securities, preferred stock, preference stock, common stock, purchase contracts, depositary shares, warrants and units in an expedited fashion. We have a commercial paper program that is an important source of inexpensive and flexible liquidity for us and a committed credit facility of \$1.0 billion to support our commercial paper issuances. The credit facility expires in April 2016 and contains affirmative and negative covenants that we believe are usual and customary for senior unsecured credit agreements, including a financial covenant requiring a maximum of a 3.5 to 1.0 adjusted leverage ratio, which is the ratio of total adjusted debt to adjusted consolidated EBITDA, as defined in the credit facility agreement. We have not drawn upon the credit facility.

At September 30, 2012, there were no outstanding commercial paper borrowings. During the quarter, commercial paper borrowings averaged \$418 million at a weighted-average interest rate of 0.48% and the maximum amount outstanding at any time was \$709 million.

In March 2012, we redeemed, at par plus accrued interest, a \$150 million term loan that was scheduled to mature in the fourth quarter of 2012 and in June 2012, we redeemed our \$400 million, 4.625% notes (the 2012 Notes) that were also scheduled to mature in the fourth quarter of 2012. As a result of the early redemption of the 2012 Notes, we recorded a net loss of \$2 million on the extinguishment of debt.

In April 2012, we entered into forward starting swap agreements with an aggregate notional value of \$150 million to hedge the interest rate risk associated with the forecasted issuance of long-term debt. The swap agreements expired prior to the issuance of debt resulting in a cash payment of \$6 million in the second quarter of 2012.

In October 2012, we borrowed \$220 million under term loan agreements. The loans bear interest at the applicable London Interbank Offered Rate (LIBOR) plus 2.25% or Prime Rate plus 1.25%, at our option. Interest is payable quarterly and the loans mature in 2015 and 2016. The proceeds from the loans will be used for general corporate purposes, including the repayment of commercial paper and 2013 debt maturities.

Cash contributions to our pension plans totaled \$8 million in the quarter and \$121 million through September 30, 2012, and includes special contributions of \$95 million. We anticipate making additional contributions of approximately \$10 million to our pension plans in the fourth quarter.

## Regulatory Matters

There have been no significant changes to the regulatory matters disclosed in our 2011 Annual Report.

Item 3: Quantitative and Qualitative Disclosures about Market Risk

There were no material changes to the disclosures made in the 2011 Annual Report regarding this matter.

Item 4: Controls and Procedures

Disclosure controls and procedures are designed to reasonably assure that information required to be disclosed in reports filed or submitted under the Securities Exchange Act of 1934, as amended (the Exchange Act) is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures are also designed to reasonably assure that such information is accumulated and communicated to our management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), as appropriate to allow timely decisions regarding required disclosure.

Under the direction of our CEO and CFO, we evaluated our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) under the Exchange Act) and internal control over financial reporting. Our CEO and CFO concluded that, as of the end of the period covered by this report, such disclosure controls and procedures were effective to ensure that information we are required to disclose in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Exchange Act. In addition, no changes in internal control over financial reporting occurred during the fiscal quarter covered by this report that have materially affected, or are reasonably likely to materially affect, such internal control over financial reporting. It should be noted that any system of controls is based in part upon certain assumptions designed to obtain reasonable (and not absolute) assurance as to its effectiveness, and there can be no assurance that any design will succeed in achieving its stated goals. Notwithstanding this caution, the disclosure controls and procedures are designed to provide reasonable assurance of achieving their stated objectives, and the CEO and CFO have concluded that the disclosure controls and procedures are effective at that reasonable assurance level.

**PART II. OTHER INFORMATION**

**Item 1: Legal Proceedings**

See Note 11 to the unaudited Condensed Consolidated Financial Statements.

**Item 1A: Risk Factors**

There were no material changes to the risk factors identified in the 2011 Annual Report.

**Item 2: Unregistered Sales of Equity Securities and Use of Proceeds**

**Repurchases of Equity Securities**

We periodically repurchase shares of our common stock to manage the dilution created by shares issued under employee stock plans and for other purposes in the open market. At September 30, 2012, we have remaining authorization to repurchase up to \$50 million of our common stock. There were no share repurchases during the quarter ended September 30, 2012.

**Item 6: Exhibits**

See Index of Exhibits.

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.

PITNEY BOWES INC.

Date: November 2, 2012

/s/ Michael Monahan

Michael Monahan  
Executive Vice President and Chief Financial Officer  
(Principal Financial Officer)

/s/ Steven J. Green

Steven J. Green  
Vice President – Finance and Chief Accounting Officer  
(Principal Accounting Officer)

Exhibit Index

| Exhibit Number | Description  | Status or incorporation by reference |
|----------------|--|--------------------------------------|
| (12)           | Computation of ratio of earnings to fixed charges  | Exhibit 12                           |
| (31.1)         | Certification of Chief Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended | Exhibit 31.1                         |
| (31.2)         | Certification of Chief Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended | Exhibit 31.2                         |
| (32.1)         | Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350  | Exhibit 32.1                         |
| (32.2)         | Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350  | Exhibit 32.2                         |
| 101.INS        | XBRL Report Instance Document  |                                      |
| 101.SCH        | XBRL Taxonomy Extension Schema Document  |                                      |
| 101.CAL        | XBRL Taxonomy Calculation Linkbase Document  |                                      |
| 101.DEF        | XBRL Taxonomy Definition Linkbase Document   |                                      |
| 101.LAB        | XBRL Taxonomy Label Linkbase Document  |                                      |
| 101.PRE        | XBRL Taxonomy Presentation Linkbase Document   |                                      |