

Dealertrack Technologies, Inc
Form 10-Q
August 06, 2013

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
b ACT OF 1934**

For the quarterly period ended June 30, 2013

OR

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

Commission File Number 000-51653

Dealertrack Technologies, Inc.

(Exact name of Registrant as specified in its charter)

Delaware

*(State or other jurisdiction of incorporation or
organization)*

52-2336218

(I.R.S. Employer Identification Number)

1111 Marcus Ave., Suite M04

Lake Success, NY 11042

(Address of principal executive offices, including zip code)

(516) 734-3600

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

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

As of July 31, 2013, 43,749,275 shares of the registrant's common stock were outstanding.

DEALERTRACK TECHNOLOGIES, INC.
FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2013

TABLE OF CONTENTS

	Page
PART I. FINANCIAL INFORMATION	3
Item 1. Financial Statements	3
Consolidated Balance Sheets as of June 30, 2013 and December 31, 2012 (Unaudited)	3
Consolidated Statements of Operations for the three and six months ended June 30, 2013 and 2012 (Unaudited)	4
Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2013 and 2012 (Unaudited)	5
Consolidated Statements of Cash Flows for the six months ended June 30, 2013 and 2012 (Unaudited)	6
Notes to Consolidated Financial Statements (Unaudited)	7
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	18
Item 3. Quantitative and Qualitative Disclosures About Market Risk	31
Item 4. Controls and Procedures	32
PART II. OTHER INFORMATION	33
Item 1. Legal Proceedings	33
Item 1A. Risk Factors	33
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	34
Item 3. Defaults Upon Senior Securities	35
Item 4. Mine Safety Disclosures	35
Item 5. Other Information	35
Item 6. Exhibits	35
Signature	36
EX-31.1: CERTIFICATION	
EX-31.2: CERTIFICATION	
EX-32.1: CERTIFICATION	

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements****DEALERTRACK TECHNOLOGIES, INC.****CONSOLIDATED BALANCE SHEETS
(Unaudited)**

	June 30, 2013	December 31, 2012
	(In thousands, except share and per share amounts)	
ASSETS		
Current assets		
Cash and cash equivalents	\$ 121,579	\$ 143,811
Marketable securities	43,808	34,031
Customer funds	5,262	1,999
Customer funds receivable	29,003	14,077
Accounts receivable, net of allowances of \$6,843 and \$4,558 as of June 30, 2013 and December 31, 2012, respectively	58,507	43,679
Deferred tax assets, net	4,412	4,412
Prepaid expenses and other current assets	26,641	19,142
Total current assets	289,212	261,151
Marketable securities – long-term	—	4,428
Property and equipment, net	31,289	27,407
Investments	121,666	122,808
Software and website development costs, net	57,457	46,182
Intangible assets, net	114,282	117,599
Goodwill	278,142	270,646
Deferred tax assets, net	43,881	43,611
Other assets — long-term	13,379	16,684
Total assets	\$ 949,308	\$ 910,516

LIABILITIES AND STOCKHOLDERS' EQUITY

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

Current liabilities		
Accounts payable	\$ 13,541	\$ 18,834
Accrued compensation and benefits	15,929	15,148
Accrued liabilities — other	22,438	16,870
Customer funds payable	34,265	16,076
Deferred revenue	8,474	7,959
Deferred tax liabilities	3,125	3,031
Due to acquirees	11,439	11,124
 Total current liabilities	 109,211	 89,042
 Deferred tax liabilities	 76,898	 77,368
Deferred revenue	5,724	5,525
Senior convertible notes, net	166,231	162,279
Other liabilities	3,636	4,985
 Total long-term liabilities	 252,489	 250,157
 Total liabilities	 361,700	 339,199
 Commitments and contingencies (Note 15)		
Stockholders' equity		
Preferred stock, \$0.01 par value: 10,000,000 shares authorized and no shares issued and outstanding	—	—
Common stock, \$0.01 par value: 175,000,000 shares authorized; 46,826,943 shares issued and 43,674,768 shares outstanding as of June 30, 2013; and 45,998,679 shares issued and 42,870,061 shares outstanding as of December 31, 2012	468	460
Treasury stock, at cost, 3,152,175 shares and 3,128,618 shares as of June 30, 2013 and December 31, 2012, respectively	(53,160)	(52,398)
Additional paid-in capital	558,590	541,948
Accumulated other comprehensive income	4,225	7,627
Retained earnings	77,485	73,680
 Total stockholders' equity	 587,608	 571,317
 Total liabilities and stockholders' equity	 \$ 949,308	 \$ 910,516

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

DEALERTRACK TECHNOLOGIES, INC.**CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(In thousands, except per share amounts)		(In thousands, except per share amounts)	
Revenue:				
Net revenue	\$121,782	\$96,396	\$230,841	\$188,013
Operating expenses:				
Cost of revenue	67,587	53,712	130,775	106,862
Product development	4,064	2,944	7,694	5,938
Selling, general and administrative	42,502	34,067	83,992	68,195
Total operating expenses	114,153	90,723	222,461	180,995
Income from operations	7,629	5,673	8,380	7,018
Interest income	117	184	241	414
Interest expense	(3,345)	(3,208)	(6,709)	(4,365)
Other income (expense), net	62	(926)	128	(850)
Gain on disposal of subsidiary and sale of other assets	—	5,500	—	33,193
Earnings from equity method investment, net	1,279	145	2,498	308
Income before provision for income taxes, net	5,742	7,368	4,538	35,718
Provision for income taxes, net	(1,903)	(1,443)	(733)	(12,832)
Net income	\$3,839	\$5,925	\$3,805	\$22,886
Basic net income per share	\$0.09	\$0.14	\$0.09	\$0.54
Diluted net income per share	\$0.09	\$0.13	\$0.09	\$0.52
Weighted average common stock outstanding (basic)	43,545	42,470	43,360	42,286
Weighted average common stock outstanding (diluted)	44,881	43,957	44,741	43,839

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

DEALERTRACK TECHNOLOGIES, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
Net income	\$3,839	\$5,925	\$3,805	\$22,886
Other comprehensive loss, net of tax				
Foreign currency translation adjustments	(2,257)	(1,136)	(3,577)	(156)
Net change in unrealized gains (losses) on securities	63	(47)	175	(14)
Other comprehensive loss, net of tax	(2,194)	(1,183)	(3,402)	(170)
Total comprehensive income	\$1,645	\$4,742	\$403	\$22,716

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

DEALERTRACK TECHNOLOGIES, INC.**CONSOLIDATED STATEMENTS OF CASH FLOWS**
(Unaudited)

	Six Months Ended June 30,	
	2013	2012
	(In thousands)	
Operating Activities:		
Net income	\$3,805	\$22,886
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	28,821	24,927
Deferred tax (benefit) provision	(653)	11,389
Stock-based compensation expense	7,126	6,712
Provision for doubtful accounts and sales credits	5,559	3,831
Earnings from equity method investment, net	(2,498)	(308)
Deferred compensation	84	75
Stock-based compensation windfall tax benefit	(4,278)	(4,108)
Gain on disposal of subsidiary and sale of other assets	—	(33,193)
Realized gain on sale of securities	(11)	—
Amortization of debt issuance costs and debt discount	4,666	2,981
Change in contingent consideration	(500)	(900)
Change in fair value of warrant	—	1,000
Amortization of deferred interest	636	164
Changes in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable	(20,535)	(7,223)
Prepaid expenses and other current assets	(4,185)	478
Other assets — long-term	7,075	4,092
Accounts payable and accrued expenses	(4,351)	(6,130)
Deferred rent	178	7
Deferred revenue	453	613
Other liabilities — long-term	(884)	(743)
Net cash provided by operating activities	20,508	26,550
Investing Activities:		
Capital expenditures	(6,112)	(4,340)
Capitalized software and website development costs	(17,360)	(9,223)
Proceeds from sale of Chrome-branded asset	—	5,500
Purchases of marketable securities	(27,231)	(70,175)
Proceeds from sales and maturities of marketable securities	21,309	4,500
Cash contributed for equity method investment	—	(1,750)
Payment for acquisition of businesses, net of acquired cash	(20,984)	—
Net cash used in investing activities	(50,378)	(75,488)

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

Financing Activities:

Principal payments on capital lease obligations and financing arrangements	(74)	(445)
Proceeds from stock purchase plan and exercise of stock options	5,295	5,451
Proceeds from issuance of senior convertible notes	—	200,000
Payments for debt issuance costs	—	(7,723)
Payments for convertible note hedges	—	(43,940)
Proceeds from issuance of warrants	—	29,740
Purchases of treasury stock	(762)	(742)
Stock-based compensation windfall tax benefit	4,278	4,108
Net cash provided by financing activities	8,737	186,449
Net (decrease) increase in cash and cash equivalents	(21,133)	137,511
Effect of exchange rate changes on cash and cash equivalents	(1,099)	(69)
Cash and cash equivalents, beginning of period	143,811	78,709
Cash and cash equivalents, end of period	\$ 121,579	\$ 216,151

Supplemental Disclosure:

Cash paid for:		
Income taxes	\$3,298	\$2,041
Interest	1,891	260
Non-cash investing and financing activities:		
Accrued capitalized hardware, software and fixed assets	5,714	1,364
Assets acquired under capital leases and financing arrangements	116	725
Non-cash consideration issued for investment in Chrome Data Solutions	—	42,301

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

DEALERTRACK TECHNOLOGIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Basis of Presentation and Business Description

Business Description

Dealertrack's web-based software solutions and services enhance efficiency and profitability for all major segments of the automotive retail industry, including dealers, lenders, OEMs, third-party retailers, agents and aftermarket providers. Dealertrack operates the largest online credit application networks in the United States and Canada. We believe Dealertrack delivers the industry's most comprehensive solution set for automotive retailers, including:

Dealer Management solutions, which provide independent and franchised dealers with a powerful dealer management system (DMS) featuring easy-to-use tools and real-time data access to enhance their efficiency;

Sales and F&I solutions, which allow dealers to streamline the in-store and online sales processes as they structure deals from a single integrated platform;

Inventory solutions, which deliver vehicle inventory management and transportation offerings to help dealers accelerate used-vehicle turn rates and assist with the facilitation of vehicle delivery;

Processing solutions, which include online motor vehicle registration, lien and titling applications and services, and collateral management services;

Digital Retailing solutions, which integrate advanced vehicle search, pricing and payment tools directly into a retailer's website; and

Interactive solutions, which deliver digital marketing and website offerings to assist dealers in achieving higher lead conversion rates by helping optimize the maximum amount of shoppers to their websites.

References in this Form 10-Q to "Dealertrack," the "Company," "our" or "we" are to Dealertrack Technologies, Inc., a Delaware corporation, and/or its subsidiaries.

Basis of Presentation

The accompanying unaudited consolidated financial statements for the three and six months ended June 30, 2013 and 2012 have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and, therefore, they do not necessarily include all information and footnotes required by accounting principles generally accepted in the United States (GAAP) for complete financial statements. The December 31, 2012 balance sheet information has been derived from the audited financial statements at that date but does not include all disclosures required by GAAP.

In the opinion of management, the unaudited financial information for the interim periods presented reflects all adjustments, which are normal and recurring, necessary for a fair presentation of the statement of results of operations, financial position, other comprehensive income and cash flows. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2012, filed with the Securities and Exchange Commission (SEC) on February 26, 2013. Operating results for the three and six months ended June 30, 2013 are not necessarily indicative of the results that may be expected for the full year ending December 31, 2013.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts and the disclosures of contingent amounts in our consolidated financial statements and the accompanying notes. Actual results could differ from those estimates.

2. Significant Accounting Policies

Our significant accounting policies are those that we believe are both important to the portrayal of our financial condition and results of operations. Management believes there have been no material changes to the significant accounting policies discussed in Note 2 of our Annual Report on Form 10-K for the year ended December 31, 2012, except as set forth below.

Stock-Based Compensation Expense and Assumptions

Expected Life

As of January 1, 2013, we determine the expected life of any issued stock-based awards based upon our historical exercise patterns and the period of time that the awards are expected to be outstanding. Previously, due to our limited public company history, the expected life was determined based upon the experience of similar entities whose shares are publicly-traded.

3. Recently Adopted Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. We adopted this update in the first quarter of 2013. The amounts reclassified out of accumulated other comprehensive income during the three and six month periods were not material.

4. Fair Value Measurements

Fair value is defined as the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Inputs used to measure fair value are prioritized into a three-level fair value hierarchy. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair values are as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 – Unobservable inputs for the asset or liability. The fair value hierarchy gives the lowest priority to Level 3 inputs.

We have segregated all financial assets that are measured at fair value on a recurring basis into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date in the table below. There were no transfers between levels of the fair value hierarchy during the periods presented below.

The fair value of our investments in debt securities, reported by the fund managers, are verified by management through the utilization of third party pricing services and review of trades completed around the period end date. We consider market liquidity in determining the fair value for these securities. After completing our validation procedures, we did not adjust any fair value measurements provided by the fund managers. These investments in debt securities are included in Level 2 of the fair value hierarchy below.

Financial assets and liabilities measured at fair value on a recurring basis include the following as of June 30, 2013 and December 31, 2012 (in thousands):

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

	Quoted Prices in	Significant Other	Significant	
As of June 30, 2013	Active Markets	Observable Inputs	Unobservable Inputs	June 30, 2013
	(Level 1)	(Level 2)	(Level 3)	
Cash equivalents (1)	\$39,805	\$—	\$—	\$39,805
Marketable securities (2)	—	43,808	—	43,808
Total	\$39,805	\$43,808	\$—	\$83,613
Contingent consideration (3)	—	—	(500) (500)
Total	\$—	\$—	\$(500) \$(500)
As of December 31, 2012	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	December 31, 2012
Cash equivalents (1)	\$63,774	\$—	\$—	\$63,774
Marketable securities (2)	—	38,459	—	38,459
Total	\$63,774	\$38,459	\$—	\$102,233
Contingent consideration (3)	—	—	(1,000) (1,000)
Total	\$—	\$—	\$(1,000) \$(1,000)

Cash equivalents consist of highly liquid investments with original maturity dates of three months or less, for (1) which we determine fair value through quoted market prices. As of June 30, 2013 and December 31, 2012, these investments were at least AA rated.

As of June 30, 2013, Level 2 marketable securities include U.S. treasury and agency securities, corporate bonds, certificates of deposit, and non-U.S. government securities. As of December 31, 2012, Level 2 marketable securities (short-term and long-term) include U.S. treasury and agency securities, corporate bonds and municipal bonds. Fair market value was determined based on the quoted market prices of the underlying securities.

In connection with our October 1, 2012 acquisition of ClickMotive, a portion of the purchase price included contingent consideration that is payable in the first quarter of 2014 based upon the achievement of certain performance targets in 2013. The fair value of the contingent consideration is determined based upon probability-weighted revenue forecasts for the underlying period. The contingent consideration is revalued each (3) reporting period, until settled, with the resulting gains and losses recorded in the consolidated statements of operations. We estimated the fair value of the contingent consideration as of June 30, 2013 to be \$0.5 million. We recorded income of \$0.5 million for the six months ended June 30, 2013 as a result of the decrease in the estimated settlement of the contingent consideration from the estimated amount of \$1.0 million as of December 31, 2012.

A reconciliation of the beginning and ending balances of the contingent consideration, a Level 3 liability, is as follows (in thousands):

Balance as of December 31, 2012	\$(1,000)
Change in fair value of contingent consideration	500
Balance as of June 30, 2013	\$(500)

Senior convertible notes

Our senior convertible notes are shown in the accompanying consolidated balance sheets at their original issuance value, net of unamortized discount, and are not marked to market. The approximate aggregate fair value of our senior convertible notes as of June 30, 2013 and December 31, 2012 was \$231.0 million and \$211.5 million, respectively. The fair value of the senior convertible notes was estimated on the basis of quoted market prices of similar securities, which, due to limited trading activity, are considered Level 2 in the fair value hierarchy.

5. Marketable Securities

Our investments in marketable securities are made within the guidelines of our investment policy, which has established guidelines relative to the diversification of our investments and their maturities, with the principle objective of capital preservation, maintaining liquidity, and avoiding concentrations.

The following is a summary of available-for-sale securities as of June 30, 2013 and December 31, 2012 (in thousands):

As of June 30, 2013	Aggregate Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Aggregate Fair Value
U.S. Treasury and agency securities	\$15,237	\$333	\$—	\$15,570
Non-U.S. government securities	5,097	—	(1) 5,096
Certificates of deposit	3,436	—	—	3,436
Corporate debt securities	19,731	0	(25) 19,706
Total	\$43,501	\$333	\$(26) \$43,808

As of December 31, 2012

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

	Aggregate Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Aggregate Fair Value
U.S. Treasury and agency securities	\$17,706	\$20	\$0	\$17,726
Corporate debt securities	20,545	20	(2) 20,563
Municipal securities	170	—	0	170
Total	\$38,421	\$40	\$(2) \$38,459

As of June 30, 2013, \$43.8 million of marketable securities had scheduled maturities of less than one year. In addition, more than half of our marketable securities were AA rated, and all securities had at least an A rating.

Investments in money market and similar short-term investments are recorded on our consolidated balance sheets as cash and cash equivalents.

Amounts reclassified out of accumulated other comprehensive income during the three and six month periods were not material.

6. Property and Equipment

Property and equipment are recorded at cost and consist of the following (dollars in thousands):

	Estimated Useful Life (Years)	June 30, 2013	December 31, 2012
Computer equipment	3 – 5	\$51,055	\$47,052
Office equipment	5	5,128	5,245
Furniture and fixtures	5	6,520	5,171
Leasehold improvements	3 – 10	6,146	4,575
Total property and equipment, gross		68,849	62,043
Less: Accumulated depreciation and amortization		(37,560)	(34,636)
Total property and equipment, net		\$31,289	\$27,407

Depreciation expense related to property and equipment for the three and six months ended June 30, 2013 was \$2.9 million and \$5.5 million, respectively, and for the three and six months ended June 30, 2012 was \$2.3 million and \$4.5 million, respectively.

7. Investments

Investments as of June 30, 2013 and December 31, 2012 consist of the following (in thousands):

	June 30, 2013	December 31, 2012
Cost method investment	\$82,690	\$82,690
Equity method investment	38,976	40,118
Total investments	\$121,666	\$122,808

Cost method investment

In consideration for the sale of ALG in 2011, we received an equity interest in TrueCar, as well as a warrant that we subsequently exercised, both of which are included within our cost method investment.

TrueCar's business simplifies and clarifies the car buying process for consumers by providing accurate market information which helps buyers make better, more informed decisions. TrueCar saves consumers time and money by providing price clarity and transparency, while delivering the benefits of higher close rates and vehicle sales to dealers. TrueCar reaches consumers via two channels – direct and indirect. The direct channel is a website that provides vehicle pricing transparency to consumers and dealers and the indirect channel is a private-label affinity buying program for major brands.

We assessed recoverability of the investment as of June 30, 2013 and do not believe this investment was impaired.

Equity method investment

We record in our consolidated statement of operations fifty percent (50%) of the net income of Chrome Data Solutions. Cash distributions, which are recorded as a reduction of our investment upon receipt, are based on a calculation considering results of operations and cash on hand. Distributions are expected to be received quarterly.

Our earnings from the equity method investment are reduced by amortization expense relating to the basis difference between the book basis of the contributed assets and the fair value of the investment recorded. This basis difference, based upon a valuation of the fair value of contributed assets, is being recorded over the lives of the underlying assets which gave rise to the basis difference, which range from 3 to 10 years. The unrecorded basis difference as of June 30, 2013 is \$10.1 million. The amortization of the basis difference to be recorded for the remainder of 2013 is \$1.4 million.

The change in our equity method investment for the three and six months ended June 30, 2013 was as follows (in thousands):

	Three Months	Six Months
	Ended June 30, 2013	Ended June 30, 2013
Beginning balance	\$40,237	\$40,118
Share of net income	1,985	3,910
Amortization of basis difference	(706)	(1,412)
Cash distributions received	(2,540)	(3,640)
Ending balance	\$38,976	\$38,976

We incur an annual data license fee payable to Chrome Data Solutions of \$0.5 million, which is recorded as cost of revenue. For the three and six months ended June 30, 2013, we accrued approximately \$0.1 million and \$0.3 million, respectively, of expense in connection with the annual data license.

Exclusive of the annual data license fee, during the three and six months ended June 30, 2013 we incurred expenses of approximately \$0.1 million and \$0.2 million, respectively, for services received and earned income of approximately \$0.1 million and \$0.1 million, respectively, for services performed, related to agreements with Chrome Data Solutions. The amounts were generally recorded as selling, general and administrative expenses and other income, respectively.

The summarized financial information of Chrome Data Solutions is presented below (in thousands):

Condensed Balance Sheet	(Unaudited) June 30, 2013	(Unaudited) December 31, 2012
Current assets	\$ 12,632	\$ 10,577
Non-current assets	33,333	34,053
Total assets	\$ 45,965	\$ 44,630
Current liabilities	\$ 6,575	\$ 5,525
Non-current liabilities	—	226
Total liabilities	\$ 6,575	\$ 5,751

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

Condensed Results of Operations	(Unaudited)		(Unaudited)	
	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenue	\$11,737	\$11,021	\$23,024	\$22,031
Gross profit	7,514	7,046	15,037	13,567
Net income	3,969	2,282	7,819	4,601

8. Intangible Assets

Intangible assets are recorded at estimated fair value and are amortized over their estimated useful lives. The gross book value, accumulated amortization and estimated useful lives of the intangible assets were as follows (dollars in thousands):

	June 30, 2013		December 31, 2012		Estimated Useful Life (Years)
	Gross Book Value	Accumulated Amortization	Gross Book Value	Accumulated Amortization	
Customer relationships	\$104,419	\$(48,440)	\$99,673	\$(43,229)	4 - 10
Technology	71,520	(28,901)	69,620	(22,369)	2 - 8
Trade names	11,000	(3,227)	9,100	(2,480)	2 - 10
Non-compete agreements	8,130	(5,466)	7,540	(4,469)	3 - 6
State DMV relationships	7,790	(2,543)	6,190	(1,977)	6 - 8
Total	\$202,859	\$(88,577)	\$192,123	\$(74,524)	

Amortization expense related to intangibles for the three and six months ended June 30, 2013 was \$7.8 million and \$15.1 million, respectively, and for the three and six months ended June 30, 2012 was \$6.7 million and \$13.5 million, respectively.

Amortization expense that will be incurred for the remaining period of 2013 and for each of the subsequent four years and thereafter is estimated as follows (in thousands):

Remainder of 2013	\$ 15,734
2014	28,522
2015	25,831
2016	16,732
2017	10,236
Thereafter	17,227
Total	\$ 114,282

9. Goodwill

The change in carrying amount of goodwill for the six months ended June 30, 2013 was as follows (in thousands):

Goodwill, gross, as of December 31, 2012	\$ 270,646
Accumulated impairment losses as of December 31, 2012	—
Goodwill, net, as of December 31, 2012	\$ 270,646
Impact of change in Canadian dollar exchange rate	(1,533)
Acquisition of Casey & Casey	9,029
Goodwill, gross, as of June 30, 2013	\$ 278,142
Accumulated impairment losses as of June 30, 2013	—
Goodwill, net, as of June 30, 2013	\$ 278,142

10. Senior Convertible Notes

On March 5, 2012, we issued \$200.0 million aggregate principal amount of 1.50% senior convertible notes in a private placement. In connection with the offering of the notes, we entered into privately negotiated convertible note hedge transactions with initial purchasers of the notes or their respective affiliates. The notes are senior unsecured obligations, subordinated in right of payment to existing and future secured senior indebtedness. We do not have the right to redeem the notes prior to maturity. The notes will mature on March 15, 2017, unless earlier repurchased or converted. For further information, see Note 19 included in our Annual Report on Form 10-K for the year ended December 31, 2012.

The net carrying amount of the liability component of the notes as of June 30, 2013 and December 31, 2012 consists of the following (in thousands):

	June 30, 2013	December 31, 2012
Principal amount	\$200,000	\$200,000
Unamortized discount	33,769	37,721
Net carrying value	\$166,231	\$162,279

Total interest expense associated with the notes consisted of the following for the three and six months ended June 30, 2013 and 2012 (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Cash interest expense (1.50% coupon rate)	\$750	\$750	\$1,500	\$958
Amortization of debt issuance costs and debt discount	2,251	2,107	4,441	2,693
Total interest expense	\$3,001	\$2,857	\$5,941	\$3,651

As of June 30, 2013, total capitalized debt issuance costs remaining to be amortized to interest expense was \$4.2 million.

As of June 30, 2013, the "if-converted value" did not exceed the principal amount of the notes since the closing share price of our common stock was less than the initial conversion price of the notes.

It is our intent to settle the par value of the notes in cash and we expect to have the liquidity to do so based upon cash on hand, net cash flows from operations, and our credit facility. As a result, there will be no potential impact to diluted earnings per share unless the share price of our stock exceeds the conversion price of \$37.37, with additional dilution if our stock price exceeds the warrant strike price of \$46.18. Subsequent to June 30, 2013, the closing share price of our common stock has exceeded the initial conversion price of the notes on several trading days.

11. Business Combinations

Casey & Casey NPS, Inc. Acquisition

On April 1, 2013, we completed the acquisition of the net assets of Casey & Casey NPS, Inc. (doing business as “Auto Title Express”) (Casey & Casey) for \$21.3 million in cash, reflective of final working capital adjustments.

Casey & Casey is Louisiana’s first electronic general public license tag agency and the largest provider of electronic vehicle registration, lien and title services, among other related services, in the state. Casey & Casey is now part of our Processing solution. This acquisition expands our transaction business and further strengthens our relationships with dealers and lenders.

We expensed approximately \$0.1 million and \$0.4 million of professional fees associated with the acquisition for the three and six months ended June 30, 2013, respectively.

This business combination was accounted for under the acquisition method of accounting, resulting in the total purchase price being allocated to the assets acquired and liabilities assumed according to their estimated fair values at the date of acquisition as follows (in thousands):

Current assets	\$5,633
Property and equipment	32
Non-current assets	15
Intangible assets	11,990
Goodwill	9,029
Total assets acquired	26,699
Total liabilities assumed	(5,387)
Net assets acquired	\$21,312

Goodwill represents the excess of the purchase price over the fair values of the acquired net tangible and intangible assets. In accordance with the provisions of FASB ASC 350, goodwill is not amortized but will be tested for impairment at least annually. The allocated value of goodwill primarily relates to the acquired workforce, as well as the anticipated synergies resulting from combining Casey & Casey with our current products and processes. Both the acquired goodwill and intangible assets are deductible for tax purposes.

The amounts allocated to acquired intangible assets, and their associated weighted-average useful lives which were determined based on the period which the assets are expected to contribute directly or indirectly to our future cash flows, consist of the following:

	Amount (In thousands)	Weighted-Average Useful Life (Years)
Customer relationships	\$ 6,000	9
Technology	1,900	4
Trade names	1,900	10
State DMV relationships	1,600	8
Non-compete agreement	590	6

Total acquired identifiable intangible assets \$ 11,990

The results of Casey & Casey were included in our consolidated statement of operations from the date of acquisition. Casey & Casey revenue, which is primarily transaction-based, was \$2.2 million from the date of acquisition through June 30, 2013. We are unable to provide Casey & Casey earnings since the date of acquisition as we do not have stand-alone earnings reporting for that business.

Unaudited Pro Forma Summary of Operations

The accompanying unaudited pro forma summary represents our consolidated results of operations as if the contribution of the net assets of Chrome to the Chrome Data Solutions joint venture and the acquisitions of Dealertrack CentralDispatch and ClickMotive had been completed as of January 1, 2011, and the acquisition of Casey & Casey had been completed as of January 1, 2012. The unaudited pro forma financial results for 2013 reflect the results for the three and six months ended June 30, 2013, as well as the effects of the pro forma adjustments for the stated transactions in 2013. The unaudited pro forma financial results for 2012 reflect the results for the three and six months ended June 30, 2012, as well as the effects of the pro forma adjustments for the stated transactions in both 2013 and 2012. Pro forma results of operations for the November 1, 2012 acquisition of the assets of Ford's iCONNECT DMS have not been presented because they are not material to the consolidated statement of operations.

The unaudited pro forma financial information includes the accounting effects of the business combinations, including adjustments to the amortization of intangible assets, professional fees associated with the transactions, and compensation expense related to amounts to be paid for continued employment. The unaudited pro forma information does not necessarily reflect the actual results that would have been achieved, nor is necessarily indicative of our future consolidated results.

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2013	2012	2013	2012
	(in thousands, except per share data)			
Net revenue	\$121,782	\$104,854	\$232,884	\$204,154
Net income	4,083	7,332	4,073	25,338
Basic net income per share	0.09	0.17	0.09	0.60
Diluted net income per share	0.09	0.17	0.09	0.58

12. Net Income Per Share

We compute net income per share in accordance with FASB ASC Topic 260, *Earnings Per Share* (ASC Topic 260). Under ASC Topic 260, basic earnings per share is calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share is calculated by dividing net income by the weighted average number of common shares outstanding, assuming dilution, during the period. The diluted earnings per share calculation assumes (i) all stock options which are in the money are exercised at the beginning of the period and (ii) if applicable, unvested awards that are considered to be contingently issuable shares because they contain either a performance or market condition will be included in diluted earnings per share if dilutive and if their conditions have (a) been satisfied at the reporting date or (b) would have been satisfied if the reporting date was the end of the contingency period.

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

The following table sets forth the computation of basic and diluted net income per share for the three and six months ended June 30, 2013 and 2012 (in thousands, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Numerator:				
Net income	\$3,839	\$5,925	\$3,805	\$22,886
Denominator:				
Weighted average common stock outstanding (basic)	43,545	42,470	43,360	42,286
Common equivalent shares from options to purchase common stock and restricted common stock units	1,336	1,487	1,381	1,553
Weighted average common stock outstanding (diluted)	44,881	43,957	44,741	43,839
Basic net income per share	\$0.09	\$0.14	\$0.09	\$0.54
Diluted net income per share	\$0.09	\$0.13	\$0.09	\$0.52

The following is a summary of the weighted shares outstanding during the respective periods that have been excluded from the diluted net income per share calculation because the effect would have been antidilutive (in thousands):

	Three Months Ended June 30, 2013		Six Months Ended June 30, 2012	
Stock options	1,043	724	850	620
Restricted stock units	11	13	253	197
Performance stock units	—	—	24	—
Total antidilutive awards	1,054	737	1,127	817

In regards to our senior convertible notes, it is our intent to settle the par value of the notes in cash, and we expect to have the liquidity to do so. As a result, there will be no potential impact to diluted earnings per share unless the share price of our stock exceeds the conversion price of \$37.37, with additional dilution if our share price exceeds the warrant strike price of \$46.18. There will be no impact to earnings per share if the impact is anti-dilutive under the if-converted method of accounting. Our share price during the three and six months ended June 30, 2013 did not exceed the conversion price or warrant strike price and therefore there was no impact to diluted net income per share. Subsequent to June 30, 2013, the closing share price of our common stock has exceeded the initial conversion price of the notes on several trading days.

13. Stock-Based Compensation Expense

Stock-based compensation is measured at the grant date, based on the fair value of the award, and recognized as an expense over the requisite service period, net of an estimated forfeiture rate. We currently have three types of stock-based compensation awards: stock options, restricted stock units and performance stock units. For further information, see Notes 2 and 14 included in our Annual Report on Form 10-K for the year ended December 31, 2012.

The following summarizes stock-based compensation expense by expense category for the three and six months ended June 30, 2013 and 2012 (in thousands):

	Three Months Ended June 30, 2013		Six Months Ended June 30, 2012	
Cost of revenue	\$786	\$590	\$1,478	\$1,225

Product development	195	206	363	420
Selling, general and administrative	2,874	2,586	5,285	5,067
Total stock-based compensation expense	\$3,855	\$3,382	\$7,126	\$6,712

14. Income Taxes

We file a consolidated U.S. income tax return and tax returns in various state and local jurisdictions. Certain of our subsidiaries also file income tax returns in Canada. The Canadian Revenue Agency is reviewing our 2009 and 2010 tax return filings. The Internal Revenue Service has concluded a review of our consolidated federal income tax returns through December 31, 2007 and is currently reviewing our consolidated federal income tax returns for 2009, 2010 and 2011. New York has concluded their review of our 2006 (amended) and 2007 state tax returns and is currently reviewing our 2008 and 2009 state returns. Our amended return filings in California and Pennsylvania are under review by each of the respective states. In addition, we are appealing Pennsylvania's assessment to our 2007, 2008 and 2009 tax return filings. All of our other significant taxing jurisdictions are closed for years prior to 2008.

The total liability recorded for uncertain tax positions that would affect our effective tax rate upon resolution of the uncertain tax position, as of June 30, 2013 and December 31, 2012, was \$0.5 million.

Interest and penalties, if any, related to tax positions taken in our tax returns are recorded in interest expense and general and administrative expenses, respectively, in our consolidated statement of operations. As of both June 30, 2013 and December 31, 2012, accrued interest and penalties related to tax positions taken on our tax returns was approximately \$0.1 million.

The net provision from income taxes for the three months ended June 30, 2013 of \$1.9 million consisted of \$0.5 million of federal income tax expense, \$0.3 million of state income tax expense and \$1.1 million of tax expense for our Canadian subsidiary.

The net provision from income taxes for the six months ended June 30, 2013 of \$0.7 million consisted of \$0.8 million of federal income tax benefit and \$1.5 million of tax expense for our Canadian subsidiary.

15. Commitments and Contingencies

Contingencies

We are a party to a variety of agreements pursuant to which we may be obligated to indemnify the other party with respect to breach of contract, infringement and other matters. Typically, these obligations arise in the context of agreements entered into by us, under which we customarily agree to hold the other party harmless against losses arising from breaches of representations, warranties and/or covenants. In these circumstances, payment by us is generally conditioned on the other party making a claim pursuant to the procedures specified in the particular agreement, which procedures typically allow us to challenge the other party's claims. Further, our obligations under these agreements may be limited to indemnification of third-party claims only and limited in terms of time and/or amount. In some instances, we may have recourse against third parties for certain payments made by us.

It is not possible to predict the maximum potential amount of future payments under these or similar agreements due to the conditional nature of our obligations and the unique facts and circumstances involved in each particular agreement. To date, we have not been required to make any material payments. We believe that if we were to incur a loss in any of these matters, it is not probable that such loss would have a material effect on our business or financial condition.

Retail Sales Tax

On an ongoing basis, various tax jurisdictions in the United States conduct reviews or audits regarding the sales taxability of our products. Historically, we have been able to respond to their inquiries without significant additional sales tax liability imposed. However, in the event we are unsuccessful in responding to future inquiries, additional sales tax liabilities may be incurred. If we are obligated to charge sales tax for certain products, we believe our contractual arrangements with our customers obligate them to pay all sales taxes that are levied or imposed by any taxing authority. We currently have \$0.9 million of pending assessments in one state. In June 2013, an administrative hearing was held on this matter and we are currently awaiting a ruling. As of June 30, 2013, we have not accrued any amounts related to this assessment. We have estimated that potential additional assessments of \$0.7 million may exist for periods subsequent to the assessment period based upon a calculation consistent with the pending assessment. We believe that our position on this matter is correct and in the event we do not prevail in the administrative hearing, we intend to appeal the matter in court.

Service Credits

Under the terms of the purchase agreement with the seller of the AAX business, the parent company of the seller was granted the right to service credits of \$2.5 million, which may be applied against fees that are charged in connection with their purchase of certain future products or services of Dealertrack. These service credits expire on December 31, 2015. The service credits are being recorded as a reduction in revenue as they are utilized. As of December 31, 2012, approximately \$0.6 million of the service credit remained. For the three and six months ended June 30, 2013, we recorded contra revenue related to the service credits of \$0.3 million and \$0.6 million, respectively. For the three and six months ended June 30, 2012, we recorded contra revenue related to the service credits of \$0.1 million and \$0.4 million, respectively.

Employment Agreements

Pursuant to employment or severance agreements with certain employees, we have a commitment to pay severance of approximately \$6.5 million as of June 30, 2013, in the event of termination without cause, as defined in the agreements, as well as certain potential gross-up payments to the extent any such severance payment would constitute an excess parachute payment under the Internal Revenue Code. Additionally, in the event of termination without cause due to a change in control, we would also have a commitment to pay additional severance of \$2.4 million as of June 30, 2013.

Legal Proceedings

From time to time, we are a party to litigation matters arising in connection with the normal course of business, none of which is expected to have a material adverse effect on us. In addition to the litigation matters arising in connection with the normal course of our business, we are party to the litigation described below.

DealerTrack, Inc. v. Finance Express et al., CV-06-2335; DealerTrack, Inc. v. RouteOne and Finance Express et al., CV-06-6864; and DealerTrack, Inc. v. RouteOne and Finance Express et al., CV-07-215

On April 18, 2006, we filed a Complaint and Demand for Jury Trial against David Huber, Finance Express LLC (Finance Express), and three of their unnamed dealer customers in the United States District Court for the Central District of California, Civil Action No. CV-06-2335 AG (FMOx). The complaint sought declaratory and injunctive relief, as well as damages, against the defendants for infringement of the U.S. Patent No. 5,878,403 (the '403 Patent) and 6,587,841 (the '841 Patent). Finance Express denied infringement and challenged the validity and enforceability of the patents-in-suit.

On October 27, 2006, we filed a Complaint and Demand for Jury Trial against RouteOne LLC (RouteOne), David Huber and Finance Express in the United States District Court for the Central District of California, Civil Action No. CV-06-6864 (SJF). The complaint sought declaratory and injunctive relief as well as damages against the

defendants for infringement of the '403 Patent and the '841 Patent. On November 28, 2006 and December 4, 2006, respectively, defendants RouteOne, David Huber and Finance Express filed their answers. The defendants denied infringement and challenged the validity and enforceability of the patents-in-suit.

On February 20, 2007, we filed a Complaint and Demand for Jury Trial against RouteOne, David Huber and Finance Express in the United States District Court for the Central District of California, Civil Action No. CV-07-215 (CWx). The complaint sought declaratory and injunctive relief as well as damages against the defendants for infringement of U.S. Patent No. 7,181,427 (the '427 Patent). On April 13, 2007 and April 17, 2007, respectively, defendants RouteOne, David Huber and Finance Express filed their answers. The defendants denied infringement and challenged the validity and enforceability of the '427 Patent.

The DealerTrack, Inc. v. Finance Express et al., CV-06-2335 action, the DealerTrack Inc. v. RouteOne and Finance Express et al., CV-06-6864 action and the DealerTrack v. RouteOne and Finance Express et al., CV-07-215 action, described above, were consolidated by the court. A hearing on claims construction, referred to as a “*Markman*” hearing, was held on September 25, 2007. Fact and expert discovery and motions for summary judgment have substantially been completed.

On July 21, 2008 and September 30, 2008, the court issued summary judgment orders disposing of certain issues and preserving other issues for trial.

On July 8, 2009, the court held Claims 1-4 on the ‘427 Patent were invalid for failure to comply with a standard required by the recently decided case in the Court of Appeals of the Federal Circuit of *In re Bilski*. On August 11, 2009, the court entered into a judgment granting summary judgment for the defendants.

On September 8, 2009, Dealertrack filed a notice of appeal in the United States Court of Appeals for the Federal Circuit in regards to the finding of non-infringement of the ‘841 Patent, the invalidity of the ‘427 Patent, and the claim construction order to the extent that it was relied upon to find the judgments of non-infringement and invalidity. The defendants also appealed certain findings of the District Court. On May 5, 2011, oral arguments on the appeal were held. On January 20, 2012, the Court of Appeals released its decision. The decision reinstated Dealertrack's infringement action against RouteOne and Finance Express on four claims of the '841 patent, found that claims 14, 16 and 17 of the ‘841 Patent were invalid for indefiniteness and upheld the District Court’s decision regarding the invalidity of certain claims of the ‘427 patent. The case was remanded to the district court for further proceedings.

On October 1, 2012, we entered into a Settlement Agreement with RouteOne which resulted in the dismissal of RouteOne from the case. The case against Finance Express remains.

We believe that the potential liability from this litigation will not have a material effect on our financial position, results of operations or cash flows when resolved in a future period.

16. Segment Information

The segment information provided in the table below is being reported consistent with our method of internal reporting. Operating segments are defined as components of an enterprise for which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The chief operating decision maker reviews information at a consolidated level, as such we

have one reportable segment. For enterprise-wide disclosure, we are organized primarily on the basis of service lines.

Revenue earned in Canada for both the three and six months ended June 30, 2013 was approximately 10% of our total net revenue. Revenue earned in Canada for the three and six months ended June 30, 2012 was approximately 11% and 10%, respectively, of our total net revenue. Long-lived assets in Canada were \$41.3 million and \$44.8 million as of June 30, 2013 and December 31, 2012, respectively.

Supplemental disclosure of revenue by service type for the three and six months ended June 30, 2013 and 2012 is as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Transaction services revenue	\$71,645	\$57,493	\$133,009	\$111,633
Subscription services revenue	44,623	33,932	87,401	67,213
Other	5,514	4,971	10,431	9,167
Total net revenue	\$121,782	\$96,396	\$230,841	\$188,013

17. Revolving Credit Facility

We have a \$125.0 million credit facility which is available for general corporate purposes (including capital expenditures and investments), subject to certain conditions. Our obligations under the credit facility are guaranteed by certain of our existing and future subsidiaries and secured by substantially all of the assets of the company and such subsidiaries. The credit facility matures on March 1, 2017. For further information, see Note 18 included in our Annual Report on Form 10-K for the year ended December 31, 2012.

Debt issuance costs associated with the credit facility amortized to interest expense for the three and six months ended June 30, 2013 were \$0.1 million and \$0.2 million, respectively. Debt issuance costs associated with the credit facility amortized to interest expense for the three and six months ended June 30, 2012 were \$0.1 million and \$0.2 million, respectively. As of June 30, 2013, there was \$1.6 million of debt issuance costs remaining to be amortized to interest expense. Interest expense related to the commitment fee for the three and six months ended June 30, 2013 was \$0.1 million and \$0.2 million, respectively. Interest expense related to the commitment fee for the three and six months ended June 30, 2012 was \$0.1 million and \$0.2 million, respectively.

As of June 30, 2013, we had no amounts outstanding under our credit facility and were in compliance with all restrictive covenants and financial ratios.

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

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with our consolidated financial statements. Certain statements in this Quarterly Report on Form 10-Q are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). These statements involve a number of risks, uncertainties and other factors that could cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. Factors that could materially affect such forward-looking statements can be found in the sections entitled "Risk Factors" in Part II, Item 1A in this Quarterly Report on Form 10-Q, as well as Part I, Item 1A in our Annual Report on Form 10-K for the year ended December 31, 2012 filed with the SEC on February 26, 2013. Investors are urged to consider these factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on such forward-looking statements. The forward-looking statements made herein are only made as of the date hereof and we undertake no obligation to publicly update such forward-looking statements to reflect subsequent events or circumstances except as required by law.

Overview

Dealertrack's web-based software solutions and services enhance efficiency and profitability for all major segments of the automotive retail industry, including dealers, lenders, OEMs, third-party retailers, agents and aftermarket providers. Dealertrack operates the largest online credit application networks in the United States and Canada. We believe Dealertrack delivers the industry's most comprehensive solution set for automotive retailers, including:

Dealer Management solutions, which provide independent and franchised dealers with a powerful dealer management system (DMS) featuring easy-to-use tools and real-time data access to enhance their efficiency;

Sales and F&I solutions, which allow dealers to streamline the in-store and online sales processes as they structure deals from a single integrated platform;

Inventory solutions, which deliver vehicle inventory management and transportation offerings to help dealers accelerate used-vehicle turn rates and assist with the facilitation of vehicle delivery;

Processing solutions, which include online motor vehicle registration, lien and titling applications and services, and collateral management services;

Digital Retailing solutions, which integrate advanced vehicle search, pricing and payment tools directly into a retailer's website; and

Interactive solutions, which deliver digital marketing and website offerings to assist dealers in achieving higher lead conversion rates by helping optimize the maximum amount of shoppers to their websites.

Executive Summary

Below are selected highlights of operations for the three months ended June 30, 2013:

On April 1, 2013, we completed the acquisition of the net assets of Casey & Casey NPS, Inc. (doing business as "Auto Title Express") (Casey & Casey) for \$21.3 million in cash, reflective of final working capital adjustments. Casey & Casey is Louisiana's first electronic general public license tag agency and the largest provider of electronic vehicle registration, lien and title services, among other related services, in the state.

Revenue for the three months ended June 30, 2013 was \$121.8 million, an increase of \$25.4 million from the three months ended June 30, 2012.

Net income for the three months ended June 30, 2013 was \$3.8 million as compared to \$5.9 million for the three months ended June 30, 2012. Net income for the three months ended June 30, 2012 was impacted by a \$3.5 million gain (net of taxes) from the sale of certain Chrome branded assets that were not contributed to the Chrome Data joint venture.

Below are selected highlights of operations for the six months ended June 30, 2013:

Revenue for the six months ended June 30, 2013 was \$230.8 million, an increase of \$42.8 million from the six months ended June 30, 2012.

Net income for the six months ended June 30, 2013 was \$3.8 million as compared to \$22.9 million for the six months ended June 30, 2012. Net income for the six months ended June 30, 2012 was positively impacted by \$16.1 million (net of tax) from a non-cash gain related to the contribution of Chrome to the Chrome Data Solutions joint venture and the \$3.5 million gain (net of taxes) from the sale of certain Chrome branded assets that were not contributed to the Chrome Data joint venture.

Non-GAAP Financial Measures and Other Business Statistics

We monitor our business performance using a number of measures that are not found in our consolidated financial statements. These measures include the number of active dealers and lenders, active lender to dealership relationships in the Dealertrack network, the number of transactions processed, average transaction price, transaction revenue per car sold, the number of subscribing dealers in the Dealertrack network, and the average monthly subscription revenue per subscribing dealership. We believe that improvements in these metrics will result in improvements in our financial performance over time.

The following table consists of our non-GAAP financial measures and certain other business statistics that management continually monitors (amounts in thousands are GAAP net income, adjusted earnings before interest, taxes, depreciation and amortization (adjusted EBITDA), adjusted net income, capital expenditure data and transactions processed):

	Three Months Ended		Six Months Ended	
	June 30, 2013	2012	June 30, 2013	2012
GAAP net income	\$3,839	\$5,925	\$3,805	\$22,886
Non-GAAP Financial Measures and Other Business Statistics:				
Adjusted EBITDA (non-GAAP) (1)	\$32,835	\$25,037	\$57,064	\$44,456
Adjusted net income (non-GAAP) (1)	\$16,702	\$13,714	\$28,738	\$23,158
Capital expenditures, software and website development costs	\$19,721	\$7,688	\$29,302	\$15,652
Active dealers in our U.S. network as of end of the period (2)	20,205	18,638	20,205	18,638
Active lenders in our U.S. network as of end of the period (3)	1,355	1,212	1,355	1,212
Active lender to dealer relationships as of end of the period (4)	184,273	177,570	184,273	177,570
Transactions processed (5)	26,176	22,562	50,282	44,313
Average transaction price (6)	\$2.79	\$2.59	\$2.70	\$2.56
Transaction revenue per car sold (7)	\$7.38	\$6.12	\$8.04	\$7.12
Subscribing dealers in U.S. and Canada as of end of the period (8)	18,076	16,280	18,076	16,280
Average monthly subscription revenue per subscribing dealership (9)	\$757	\$697	\$747	\$693

- (1) Adjusted EBITDA is a non-GAAP financial measure that represents GAAP net income (loss) excluding interest, taxes, depreciation and amortization expenses, stock-based compensation, contra-revenue and certain items, as applicable, such as: impairment charges, restructuring charges, impact of acquisition-related activity (including contingent consideration changes, compensation expense, basis difference amortization, and professional service fees), realized gains on sales of previously impaired securities, gains or losses on sales or disposals of subsidiaries and other assets, rebranding expenses and certain other non-recurring items.

Adjusted net income is a non-GAAP financial measure that represents GAAP net income (loss) excluding stock-based compensation expense, the amortization of acquired identifiable intangibles, contra-revenue, and certain items, as applicable, such as: impairment charges, restructuring charges, impact of acquisition-related activity (including contingent consideration changes, compensation expense, basis difference amortization, and professional service fees), realized gains on sales of previously impaired securities, gains or losses on sales or disposals of subsidiaries and other assets, adjustments to deferred tax asset valuation allowances, non-cash interest expense, rebranding expenses and certain other non-recurring items. These adjustments to net income (loss), which are shown before taxes, are adjusted for their tax impact at their applicable statutory rates.

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

Adjusted EBITDA and adjusted net income are presented because management believes that they provide additional information with respect to the performance of our fundamental business activities and are also frequently used by securities analysts, investors and other interested parties in the evaluation of comparable companies. We rely on adjusted EBITDA and adjusted net income as primary measures to review and assess the operating performance of our company and management team in connection with our executive compensation plan incentive payments.

Adjusted EBITDA and adjusted net income have limitations as analytical tools and you should not consider them in isolation from, or as a substitute for, analysis of our results as reported under GAAP. Some of these limitations are:

- Adjusted EBITDA and adjusted net income do not reflect our cash expenditures or future requirements for capital expenditures or contractual commitments;

- Adjusted EBITDA and adjusted net income do not reflect changes in, or cash requirements for, our working capital needs;

- Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and adjusted EBITDA and adjusted net income do not reflect any cash requirements for such replacements;

- Non-cash compensation is and will remain a key element of our overall long-term incentive compensation package, although we exclude it from adjusted net income and adjusted EBITDA when evaluating our ongoing performance for a particular period;

- Adjusted EBITDA and adjusted net income do not reflect the impact of certain charges or gains resulting from matters we consider not to be indicative of our ongoing operations; and

- Other companies may calculate adjusted EBITDA and adjusted net income differently than we do, limiting its usefulness as a comparative measure.

Because of these limitations, adjusted EBITDA and adjusted net income should not be considered as measures of discretionary cash available to us to invest in the growth of our business. We compensate for these limitations by relying primarily on our GAAP results and using adjusted EBITDA and adjusted net income only as supplements to our GAAP results. Adjusted EBITDA and adjusted net income are measures of our performance that are not required by, or presented in accordance with, GAAP. Adjusted EBITDA and adjusted net income are not measurements of our financial performance under GAAP and should not be considered as alternatives to net income, operating income or any other performance measures derived in accordance with GAAP or as alternatives to cash flow from operating activities as a measure of our liquidity.

The following table sets forth the reconciliation of adjusted EBITDA, a non-GAAP financial measure, from net income, our most directly comparable financial measure, in accordance with GAAP (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
GAAP net income	\$3,839	\$5,925	\$3,805	\$22,886
Interest income	(117)	(184)	(241)	(414)
Interest expense – cash	981	988	2,043	1,442
Interest expense – non-cash (10)	2,364	2,220	4,666	2,923
Provision for income taxes, net	1,903	1,443	733	12,832
Depreciation of property and equipment and amortization of capitalized software and website costs	7,165	6,295	13,746	11,395
Amortization of acquired identifiable intangibles	7,759	6,653	15,075	13,532
EBITDA (non-GAAP)	23,894	23,340	39,827	64,596
Adjustments:				
Stock-based compensation	3,855	3,382	7,126	6,712
Contra-revenue (11)	1,381	996	2,735	2,098
Acquisition-related and other professional fees	573	538	1,056	737
Acquisition-related contingent consideration changes and compensation expense, net (12)	594	(220)	629	(42)
Integration and other related costs	1,567	221	2,366	221
Gain on disposal of subsidiary and sale of other assets	—	(5,500)	—	(33,193)
Amortization of equity method investment basis difference (13)	706	996	1,412	1,993
Rebranding expense	265	284	1,913	334
Change in fair value of warrant	—	1,000	—	1,000
Adjusted EBITDA (non-GAAP)	\$32,835	\$25,037	\$57,064	\$44,456

The following table sets forth the reconciliation of adjusted net income, a non-GAAP financial measure, from net income, our most directly comparable financial measure in accordance with GAAP (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
GAAP net income	\$3,839	\$5,925	\$3,805	\$22,886
Adjustments:				
Interest expense – non-cash (not tax-impacted) (10)	2,364	2,220	4,666	2,923
Amortization of acquired identifiable intangibles	7,759	6,653	15,075	13,532
Stock-based compensation	3,855	3,382	7,126	6,712
Contra-revenue (11)	1,381	996	2,735	2,098
Gain on disposal of subsidiary and sale of other assets	—	(5,500)	—	(33,193)
Acquisition-related and other professional fees	573	538	1,056	737
Acquisition-related contingent consideration changes and compensation expense, net (12)	594	(220)	629	(42)
Integration and other related costs	1,810	221	2,609	221
Rebranding expense	265	284	1,913	334
Amortization of equity method investment basis difference (13)	706	996	1,412	1,993
Accelerated depreciation of certain technology assets (14)	—	929	—	929
Change in fair value of warrant	—	1,000	—	1,000
Amended state tax returns impact (non-taxable)	—	—	56	—
Tax impact of adjustments (15)	(6,444)	(3,710)	(12,344)	3,028
Adjusted net income (non-GAAP)	\$16,702	\$13,714	\$28,738	\$23,158

(2) We consider a dealer to be active in our U.S. network as of a date if the dealer completed at least one revenue-generating credit application processing transaction using the U.S. Dealertrack network during the most recently ended calendar month. The number of active U.S. dealers is based on the number of dealer accounts as communicated by lenders on the U.S. Dealertrack network.

(3) We consider a lender to be active in our U.S. network as of a date if it is accepting credit application data electronically from U.S. dealers in the U.S. Dealertrack network.

(4) Each lender to dealer relationship represents a pair between an active U.S. lender and an active U.S. dealer at the end of a given period.

(5) Represents revenue-generating transactions processed in the U.S. Dealertrack, Dealertrack Aftermarket Services, Dealertrack Processing Solutions and Dealertrack Canada networks at the end of a given period.

(6) Represents the average revenue earned per transaction processed in the U.S. Dealertrack, Dealertrack Aftermarket Services, Dealertrack Processing Solutions and Dealertrack Canada networks during a given period. Revenue used in the calculation adds back (excludes) transaction related contra-revenue.

(7)

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

Represents transaction services revenue divided by our estimate of total new and used car sales for the period in the U.S. and Canada. Revenue used in this calculation adds back (excludes) transaction related contra-revenue.

(8) Represents the number of dealerships in the U.S. and Canada with one or more active subscriptions at the end of a given period. Subscriptions to Dealertrack CentralDispatch have been excluded as their customers include brokers and carriers in addition to dealers.

(9) Represents subscription services revenue divided by average subscribing dealers for a given period in the U.S. and Canada. Revenue used in the calculation adds back (excludes) subscription related contra-revenue. In addition, subscribing dealers and subscription services revenue from Dealertrack CentralDispatch have been excluded from the calculation as a majority of these customers are not dealers.

(10) Represents interest expense relating to the amortization of deferred financing costs and debt discount in connection with the senior convertible notes and revolving credit facility.

(11) For further information, please refer to Note 15 in the accompanying notes to the consolidated financial statements included in this Quarterly Report on Form 10-Q and Note 15 and Note 17 in the notes to the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2012.

- (12) Represents the change in the acquisition-related contingent consideration from the eCarList and ClickMotive acquisitions and other additional acquisition-related compensation charges.
- (13) Represents amortization of the basis difference between the book basis of the Chrome assets contributed to the Chrome Data Solutions joint venture and the fair value of the investment in Chrome Data Solutions.
- (14) Represents the accelerated depreciation of certain technology assets due to the discontinuation of those projects.

The tax impact of adjustments for the three and six months ended June 30, 2013 are based on a U.S. statutory tax rate of 38.2% applied to taxable adjustments other than amortization of acquired identifiable intangibles and stock-based compensation expense, which are based on a blended tax rate of 38.1% and 37.8%, respectively, for the three months ended June 30, 2013, and 38.1% and 37.7%, respectively, for the six months ended June 30, (15) 2013. The tax impact of adjustments for the three and six months ended June 30, 2012 were based on a U.S. statutory tax rate of 37.4% applied to taxable adjustments other than amortization of acquired identifiable intangibles and stock-based compensation expense, which are based on a blended tax rate of 37.3% and 36.8%, respectively, for the three months ended June 30, 2012, and 37.3% and 36.9%, respectively, for the six months ended June 30, 2012.

Revenue

Transaction Services Revenue. Transaction services revenue consists of revenue earned from our lender customers for each credit application or contract that dealers submit to them. In addition, we earn transaction services revenue from lender customers for each financing contract executed via our electronic contracting and digital contract processing solutions as well as from lender customers for collateral management transactions.

We also earn transaction services revenue from dealers or other service and information providers, such as aftermarket providers, accessory providers and credit report providers, for each fee-bearing product accessed by dealers. This includes transaction services revenue for completion of on-line registrations with department of motor vehicles, completion of inventory appraisals, and accessing of credit reports.

Subscription Services Revenue. Subscription services revenue consists of revenue earned from our dealers and other customers (typically on a monthly basis) for use of our subscription or license-based products and services. Our subscription services enable dealers and other customers to manage their dealership data and operations, compare various financing and leasing options and programs, sell insurance and other aftermarket products, analyze, merchandise, and transport inventory and execute financing contracts electronically.

Other Revenue. Other revenue consists of revenue primarily earned through forms programming, data conversion, hardware and equipment sales from our Dealer Management solution, shipping fees and commissions earned from our

digital contract business. Training fees are also included in other revenue.

Operating Expenses

Cost of Revenue. Cost of revenue primarily consists of expenses related to running our network infrastructure (including Internet connectivity, hosting expenses, and data storage), amortization expense on acquired intangible assets, capitalized software and website development costs, compensation and related benefits for network and technology development personnel, amounts paid to third parties pursuant to contracts under which (i) a portion of certain revenue is owed to those third parties (revenue share) or, (ii) fees are due on the number of transactions processed and direct costs for data licenses. Cost of revenue also includes hardware costs associated with our DMS product offering, and compensation, related benefits and travel expenses associated with DMS installation personnel, compensation and related benefits associated with strategic inventory consulting personnel, compensation and related benefits, and temporary labor associated with personnel who process transactions for our digital contract, collateral management, and registration and titling solutions, and advertising expenses associated with certain of our search and media product offerings.

Product Development Expenses. Product development expenses consist primarily of compensation and related benefits, consulting fees and other operating expenses associated with our product development departments. The product development departments perform research and development, in addition to enhancing and maintaining existing products.

Selling, General and Administrative Expenses. Selling, general and administrative expenses consist primarily of compensation and related benefits, facility costs, professional services fees for our sales, marketing, customer service and administrative functions, and public company costs.

We allocate overhead such as occupancy and telecommunications charges, and depreciation expense based on headcount, as we believe this to be the most accurate measure. As a result, a portion of general overhead expenses are reflected in each operating expense category.

Acquisitions

On April 1, 2013, we completed the acquisition of the net assets of Casey & Casey for \$21.3 million in cash, reflective of final working capital adjustments. For further information, please refer to Note 11 in the accompanying notes to the consolidated financial statements included in this Quarterly Report on Form 10-Q.

Fair Value Measurements

We have segregated all financial assets that are measured at fair value on a recurring basis into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date.

A reconciliation of the beginning and ending balances of the contingent consideration, a Level 3 liability, is as follows (in thousands):

Balance as of December 31, 2012	\$(1,000)
Change in fair value of contingent consideration	500
Balance as of June 30, 2013	\$(500)

In connection with our October 1, 2012 acquisition of ClickMotive, a portion of the purchase price included contingent consideration that is payable in the first quarter of 2014 based upon the achievement of certain performance targets in 2013. The fair value of the contingent consideration is determined based upon probability-weighted revenue forecasts for the underlying period. The contingent consideration is revalued each reporting period, until settled, with the resulting gains and losses recorded in the consolidated statements of operations. We estimated the fair value of the contingent consideration as of June 30, 2013 to be \$0.5 million. We recorded income of \$0.5 million for the six months ended June 30, 2013 as a result of the decrease in the estimated settlement of the contingent consideration from the estimated amount of \$1.0 million as of December 31, 2012.

Critical Accounting Policies and Estimates

Our management’s discussion and analysis of our financial condition and results of our operations is based on our consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these consolidated financial statements requires management to make estimates and judgments that affect the amounts reported for assets, liabilities, revenue, expenses and the disclosure of contingent liabilities.

Our critical accounting policies are those that we believe are both important to the portrayal of our financial condition and results of operations and that involve difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. The estimates are based on historical experience and on various assumptions about the ultimate outcome of future events. Our actual results may differ from these estimates. Management believes there have been no material changes to the critical accounting policies discussed in the section entitled “Management Discussion and Analysis of Financial Condition and Results of

Operations” in our Annual Report on Form 10-K for the year ended December 31, 2012, except as set forth below.

Stock-Based Compensation Expense and Assumptions

Expected Life

As of January 1, 2013, we determine the expected life of any issued stock-based awards based upon our historical exercise patterns and the period of time that the awards are expected to be outstanding. Previously, due to our limited public company history, the expected life was determined based upon the experience of similar entities whose shares are publicly-traded.

Results of Operations

The following table sets forth, for the periods indicated, the consolidated statements of operations:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2013		2012		2013		2012	
	\$	% of	\$	% of	\$	% of	\$	% of
	Amount	Net	Amount	Net	Amount	Net	Amount	Net
		Revenue		Revenue		Revenue		Revenue
	(In thousands, except percentages)				(In thousands, except percentages)			
Consolidated Statements of Operations Data:								
Net revenue	\$ 121,782	100 %	\$ 96,396	100 %	\$ 230,841	100 %	\$ 188,013	100 %
Operating expenses:								
Cost of revenue	67,587	56	53,712	56	130,775	57	106,862	57
Product development	4,064	3	2,944	3	7,694	3	5,938	3
Selling, general and administrative	42,502	35	34,067	35	83,992	36	68,195	36
Total operating expenses	114,153	94	90,723	94	222,461	96	180,995	96
Income from operations	7,629	6	5,673	6	8,380	4	7,018	4
Interest income	117	—	184	0	241	0	414	0
Interest expense	(3,345)	(3)	(3,208)	(3)	(6,709)	(3)	(4,365)	(2)
Other income (expense), net	62	—	(926)	(1)	128	0	(850)	(1)
Gain on disposal of subsidiary and sale of other assets	—	—	5,500	6	—	—	33,193	18
Earnings from equity method investment, net	1,279	2	145	0	2,498	1	308	0
Income before provision for income taxes, net	5,742	5	7,368	8	4,538	2	35,718	19
Provision for income taxes, net	(1,903)	(2)	(1,443)	(2)	(733)	0	(12,832)	(7)
Net income	\$ 3,839	3 %	\$ 5,925	6 %	\$ 3,805	2 %	\$ 22,886	12 %

Three Months Ended June 30, 2013 and 2012

Revenue

	Three Months Ended June 30,		Variance		
	2013	2012	\$ Amount	Percent	
	(In thousands, except percentages)				
Transaction services revenue	\$71,645	\$57,493	\$14,152	25	%
Subscription services revenue	44,623	33,932	10,691	32	%
Other	5,514	4,971	543	11	%
Total net revenue	\$121,782	\$96,396	\$25,386	26	%

Transaction Services Revenue. The increase in transaction services revenue is primarily due to the improving credit availability, increased application activity, and an increase in automobile sales. These industry trends had a positive impact on the following changes in our key business metrics.

	Three Months Ended June 30,		Variance		
	2013	2012	Amount	Percent	
Average transaction price (1)	\$2.79	\$2.59	\$0.20	8	%
Transaction revenue per car sold	\$7.38	\$6.12	\$1.26	21	%
Active lenders in our U.S. network as of end of the period	1,355	1,212	143	12	%
Active lender to dealer relationships as of end of the period	184,273	177,570	6,703	4	%
Transactions processed (in thousands, except percentages)	26,176	22,562	3,614	16	%

(1)- Revenue used in the calculation adds back (excludes) contra revenue.

Our average transaction price and the total number of transactions processed increased 8% and 16%, respectively, which resulted in an increase in revenue of \$5.1 million and \$9.4 million, respectively, offset by additional contra-revenue of \$0.3 million. Contributing factors to the increase in average transaction price and the total number of transactions processed included increases of 12% in active lender customers in our U.S. Dealertrack network and a 4% increase in our active lender to dealer relationships, as well as an increase in car sales volumes. While new lender customers are generally lower transaction volume customers, they have higher average prices per transaction. Additional volumes at Dealertrack Processing solutions, which are at higher average price than our other transactions, also contributed to the increase. The increase in our number of lender to dealer relationships was attributable to more active dealers, more active lenders on our U.S. network, and an increase in the average number of lenders that dealers use. In addition, expanded use across our range of transaction products increased our transaction revenue per car sold. The Casey & Casey acquisition contributed \$2.1 million to transaction services revenue for the three months ended June 30, 2013.

Subscription Services Revenue. The increase in subscription services revenue is primarily a result of additional subscription services revenue from the acquisitions of Dealertrack CentralDispatch on August 1, 2012 and ClickMotive on October 1, 2012, and organic growth. The net increase in subscription services revenue was a result of the following changes in our key business metrics.

	Three Months Ended June 30,		Variance	
	2013	2012	Amount	Percent
Average monthly subscription revenue per subscribing dealership (1)(2)	\$757	\$697	\$60	9 %
Subscribing dealers in U.S. and Canada as of end of the period (2)	18,076	16,280	1,796	11 %

(1)- Revenue used in the calculation adds back (excludes) contra revenue.

(2) - Subscribing dealers and subscription revenue from Dealertrack CentralDispatch have been excluded from the calculation as a majority of these customers are not dealers.

Our average monthly subscription revenue per subscribing dealer and the number of subscribing dealers increased 9% and 11%, respectively. The Dealertrack CentralDispatch and ClickMotive acquisitions contributed \$8.7 million in total to subscription services revenue. Their acquired quarterly subscription services revenue upon acquisition was \$6.8 million. In addition, we had continued success in selling DMS and Sales and F&I products, including our ability to cross sell those solutions to existing customers, which increased the average monthly spend per subscribing dealer.

Other Revenue. The increase in other revenue resulted from increased training revenue, primarily from our DMS solution.

Operating Expenses

	Three Months Ended June 30,		Variance		
	2013	2012	\$ Amount	Percent	
	(In thousands, except percentages)				
Cost of revenue	\$67,587	\$53,712	\$13,875	26	%
Product development	4,064	2,944	1,120	38	%
Selling, general and administrative	42,502	34,067	8,435	25	%
Total operating expenses	\$114,153	\$90,723	\$23,430	26	%

Cost of Revenue. The increase was primarily the result of \$4.2 million of additional compensation and related benefit costs and \$2.6 million in additional technology expenses, including technology consulting and other related expenses, primarily due to additional team members, including those from the acquisitions of Casey & Casey, Dealertrack CentralDispatch and ClickMotive.

There were also increases in direct costs of revenue of \$1.8 million for Processing solutions (volume related), \$1.6 million for ClickMotive (acquired in October 2012), and \$0.4 million for DMS. Other increases included \$1.2 million of intangible amortization expense, \$1.0 million of amortization of software development costs, \$0.8 million of occupancy and telecom costs, and \$0.4 million in depreciation expense. The increase in intangible amortization expense is primarily a result of additional acquired intangibles from acquisitions. The additional occupancy and telecom costs are a result of incremental team members and facilities, including those from acquisitions, as well as \$0.3 million of rent acceleration as a result of vacating the former ClickMotive office space.

Product Development Expenses. The increase was primarily the result of an increase of \$1.0 million in compensation and related benefit costs primarily due to additional team members, including those from acquisitions.

Selling, General and Administrative Expenses. The increase was primarily the result of \$5.1 million of additional compensation and related benefit costs, primarily due to additional team members, including those from acquisitions.

There were also increases of \$0.6 million in occupancy and telecom costs, which are primarily acquisition-related, \$0.6 million in bad debt expense, \$0.4 million in travel and related costs, \$0.3 million in professional fees, including acquisition and integration costs, and \$0.3 million of general and administrative costs from Casey & Casey and ClickMotive. These increases were offset by two prior period items that net to an additional \$0.3 million for the three months ended June 30, 2012. The prior period included \$1.0 million in accelerated depreciation for discontinued technology, which was offset by income of \$0.7 million related to the reduction in the eCarList contingent consideration.

Interest Expense

	Three Months Ended June 30,		Variance	
	2013	2012	\$ Amount	Percent
	(In thousands, except percentages)			
Interest expense	\$(3,345)	\$(3,208)	\$(137)	4 %

Interest expense related to the notes for the three months ended June 30, 2013 consisted of coupon interest of \$0.8 million, amortization of debt discount of \$2.0 million, and amortization of debt issuance costs of \$0.2 million. Interest expense related to our revolving credit facility for the three months ended June 30, 2013 consisted of commitment fees of \$0.1 million and amortization of debt issuance costs of \$0.1 million.

Other Income (Expense), net

	Three Months Ended June 30,		Variance	
	2013	2012	\$ Amount	Percent
	(In thousands, except percentages)			
Other income (expense), net	\$62	\$(926)	\$988	(107)%

The increase in other income (expense), net is primarily due to a \$1.0 million decrease in the estimated value of our warrant in TrueCar during the three months ended June 30, 2012.

Gain on Disposal of Subsidiary and Sale of Other Assets

Three Months Ended June 30, 2012	Variance
	Percent

	\$ Amount (In thousands, except percentages)		
Gain on disposal of subsidiary and sale of other assets	\$—\$5,500	\$(5,500)	(100)%

During the three months ended June 30, 2012, we recorded a gain of \$5.5 million related to the sale of a Chrome-branded asset.

Earnings from Equity Method Investment, Net

	Three Months Ended June 30,		Variance	
	2013	2012	\$ Amount	Percent
Earnings from equity method investment, net	\$1,279	\$145	\$1,134	782 %

(In thousands, except percentages)

During the three months ended June 30, 2013, we recorded net earnings from the Chrome Data Solutions joint venture of \$1.3 million, as compared to \$0.1 million for the three months ended June 30, 2012. The net earnings for the three months ended June 30, 2013 consisted of our 50% share of the joint venture net income of \$2.0 million, which was reduced by approximately \$0.7 million of basis difference amortization. The net earnings for the three months ended June 30, 2012 consisted of our 50% share of the joint venture net income of \$1.1 million, which was reduced by approximately \$1.0 million of basis difference amortization.

Provision for Income Taxes, Net

	Three Months Ended June 30,		Variance	
	2013	2012	\$ Amount	Percent
Provision for income taxes, net	\$(1,903)	\$(1,443)	\$(460)	32 %

(In thousands, except percentages)

The net provision for income taxes for the three months ended June 30, 2013 of \$1.9 million consisted of \$0.5 million of federal income tax expense, \$0.3 million of state income tax expense and \$1.1 million of tax expense for our Canadian subsidiary. The state income tax expense includes \$0.2 million of deferred tax expense which resulted from a change in state apportionment due to the acquisition of Casey & Casey.

The net provision for income taxes for the three months ended June 30, 2012 of \$1.4 million consisted of \$1.0 million of federal income tax expense, \$0.5 million of state income tax benefit and \$0.9 million of tax expense for our Canadian subsidiary. Included in our tax expense for our U.S. subsidiaries for the three months ended June 30, 2012 was income tax provision of \$2.0 million on the gain recorded in connection with the sale of a Chrome-branded asset, and \$0.2 million of a reduction in valuation allowance resulting from the asset sale, and \$0.4 million of benefit on the change in value of our warrant in TrueCar.

Our effective tax rate for the three months ended June 30, 2013 is 33.2% compared with 19.6% for the three months ended June 30, 2012.

Six Months Ended June 30, 2013 and 2012**Revenue**

	Six Months Ended June 30,		Variance		
	2013	2012	\$ Amount	Percent	
	(In thousands, except percentages)				
Transaction services revenue	\$133,009	\$111,633	\$21,376	19	%
Subscription services revenue	87,401	67,213	20,188	30	%
Other	10,431	9,167	1,264	14	%
Total net revenue	\$230,841	\$188,013	\$42,828	23	%

Transaction Services Revenue. The increase in transaction services revenue is primarily due to the improving credit availability, increased application activity, and an increase in automobile sales. These industry trends had a positive impact on the following changes in our key business metrics.

	Six Months Ended June 30,		Variance		
	2013	2012	Amount	Percent	
Average transaction price (1)	\$2.70	\$2.56	\$0.14	5	%
Transaction revenue per car sold	\$8.04	\$7.12	\$0.92	13	%
Active lenders in our U.S. network as of end of the period	1,355	1,212	143	12	%
Active lender to dealer relationships as of end of the period	184,273	177,570	6,703	4	%
Transactions processed (in thousands, except percentages)	50,282	44,313	5,969	13	%

(1)- Revenue used in the calculation adds back (excludes) contra revenue.

Our average transaction price and the total number of transactions processed increased 5% and 13%, respectively, which resulted in an increase in revenue of \$6.8 million and \$15.3 million, respectively, offset by additional contra-revenue of \$0.7 million. Contributing factors to the increase in average transaction price and the total number of transactions processed included increases of 12% in active lender customers in our U.S. Dealertrack network and a 4% increase in our active lender to dealer relationships, as well as an increase in car sales volumes. While new lender customers are generally lower transaction volume customers, they have higher average prices per transaction. Additional volumes at Dealertrack Processing solutions, which are at higher average price than our other transactions, also contributed to the increase. The increase in our number of lender to dealer relationships was attributable to more active dealers, more active lenders on our U.S. network, and an increase in the average number of lenders that dealers

use. In addition, expanded use across our range of transaction products increased our transaction revenue per car sold. The Casey & Casey acquisition contributed \$2.1 million to transaction services revenue for the six months ended June 30, 2013.

Subscription Services Revenue. The increase in subscription services revenue is primarily a result of additional subscription services revenue from the acquisitions of Dealertrack CentralDispatch on August 1, 2012 and ClickMotive on October 1, 2012 and organic growth. The net increase in subscription services revenue was a result of the following changes in our key business metrics.

	Six Months Ended		Variance	
	June 30, 2013	2012	Amount	Percent
Average monthly subscription revenue per subscribing dealership (1)(2)	\$747	\$693	\$54	8 %
Subscribing dealers in U.S. and Canada as of end of the period (2)	18,076	16,280	1,796	11 %

(1)- Revenue used in the calculation adds back (excludes) contra revenue.

(2) - Subscribing dealers and subscription revenue from Dealertrack CentralDispatch have been excluded from the calculation as a majority of these customers are not dealers.

Our average monthly subscription revenue per subscribing dealer and the number of subscribing dealers increased 8% and 11%, respectively. The Dealertrack CentralDispatch and ClickMotive acquisitions contributed \$16.8 million in total to subscription services revenue. Their acquired quarterly subscription services revenue upon acquisition was \$6.8 million (\$13.6 million for six-months). In addition, we had continued success in selling DMS and Sales and F&I products, including our ability to cross sell those solutions to existing customers, which increased the average monthly spend per subscribing dealer.

Other Revenue. The increase in other revenue resulted from increased training revenue, primarily from our DMS solution.

Operating Expenses

	Six Months Ended June 30,		Variance		
	2013	2012	\$ Amount	Percent	
	(In thousands, except percentages)				
Cost of revenue	\$130,775	\$106,862	\$23,913	22	%
Product development	7,694	5,938	1,756	30	%
Selling, general and administrative	83,992	68,195	15,797	23	%
Total operating expenses	\$222,461	\$180,995	\$41,466	23	%

Cost of Revenue. The increase was primarily the result of \$6.7 million of additional compensation and related benefit costs and \$5.7 million in additional technology expenses, including technology consulting and other related expenses, primarily due to additional team members from the acquisitions of Casey & Casey, Dealertrack CentralDispatch, and ClickMotive.

There were also increases in direct costs of revenue of \$3.1 million for ClickMotive (acquired in October 2012), \$2.8 million for Processing solutions (volume related), and \$0.6 million for DMS. Other increases included \$2.0 million of amortization of software development costs, \$1.7 million of intangible amortization expense, \$1.1 million in occupancy and telecom costs, and \$0.6 million in depreciation expense. The increase in intangible amortization expense is primarily a result of additional acquired intangibles from acquisitions. The additional occupancy and telecom costs are a result of incremental team members and facilities, including those from acquisitions, as well as \$0.3 million of rent acceleration as a result of vacating the former ClickMotive office space.

Product Development Expenses. The increase was primarily the result of an increase of \$1.6 million in compensation and related benefit costs primarily due to additional team members, including those from acquisitions.

Selling, General and Administrative Expenses. The increase was primarily the result of an increase of \$10.1 million in compensation and related benefit costs primarily due to additional team members, including those from acquisitions.

There were additional increases of \$1.6 million in marketing and rebranding, \$0.9 million in occupancy and telecom costs (primarily acquisition-related), \$0.8 million in professional fees (including acquisition and integration costs), \$0.6 million in travel and related costs, \$0.4 million of general and administrative costs from the Casey & Casey and ClickMotive acquisitions, and \$0.4 million in depreciation expense. Marketing costs included expenses related to the rebranding, including costs related to the launch of our newly rebranded comprehensive suite of technologies at

National Automobile Dealers Association (NADA), our industry's largest trade event. These increases were offset by two prior period items that net to an additional \$0.6 million for the six months ended June 30, 2013, \$1.0 million in accelerated depreciation for discontinued technology and incremental contingent consideration reduction of \$0.4 million.

Interest Expense

Six Months Ended June 30,		Variance	
2013	2012	\$ Amount	Percent
(In thousands, except percentages)			
Interest expense	\$(6,709)	\$(4,365)	\$(2,344) 54 %

Interest expense related to the notes for the six months ended June 30, 2013 consisted of coupon interest of \$1.5 million, amortization of debt discount of \$4.0 million, and amortization of debt issuance costs of \$0.5 million. Interest expense related to our revolving credit facility for the six months ended June 30, 2013 consisted of commitment fees of \$0.2 million and amortization of debt issuance costs of \$0.2 million.

Other Income (Expense), Net

Six Months Ended June 30,		Variance	
2013	2012	\$ Amount	Percent
(In thousands, except percentages)			
Other income (expense), net	\$128	\$(850)	\$978 (115)%

The increase in other income (expense), net is primarily due to a \$1.0 million decrease in the estimated value of our warrant in TrueCar during the six months ended June 30, 2012.

Gain on Disposal of Subsidiary and Sale of Other Assets

	Six Months Ended June 30,		Variance	
	2013	2012	\$ Amount	Percent
	(In thousands, except percentages)			
Gain on disposal of subsidiary and sale of other assets	\$—	\$33,193	\$(33,193)	(100)%

During the six months ended June 30, 2012, we recorded a gain on the contribution of the net assets of Chrome to the Chrome Data Solutions joint venture in the amount of \$27.7 million and a gain of \$5.5 million related to the sale of a Chrome-branded asset, which was not contributed to the joint venture.

Earnings from Equity Method Investment, Net

	Six Months Ended June 30,		Variance	
	2013	2012	\$ Amount	Percent
	(In thousands, except percentages)			
Earnings from equity method investment, net	\$2,498	\$308	\$2,190	711 %

During the six months ended June 30, 2013, we recorded net earnings from the Chrome Data Solutions joint venture of \$2.5 million, as compared to \$0.3 million for the six months ended June 30, 2012. The net earnings for the six months ended June 30, 2013 consisted of our 50% share of the joint venture net income of \$3.9 million, which was reduced by approximately \$1.4 million of basis difference amortization. The net earnings for the six months ended June 30, 2012 consisted of our 50% share of the joint venture net income of \$2.3 million, which was reduced by approximately \$2.0 million of basis difference amortization.

Provision for Income Taxes, net

Variance

Edgar Filing: Dealertrack Technologies, Inc - Form 10-Q

Six Months Ended June 30,			
2013	2012	\$ Amount	Percent
(In thousands, except percentages)			
Provision for income taxes, net	\$(733)	\$(12,832)	\$12,099 (94)%

The net provision for income taxes for the six months ended June 30, 2013 of \$0.7 million consisted of \$0.8 million of federal income tax benefit and \$1.5 million of tax expense for our Canadian subsidiary. The state income tax expense includes \$0.2 million of deferred tax expense which resulted from a change in state apportionment due to the acquisition of Casey & Casey. The federal income tax benefit includes a \$0.4 million benefit from research and development credits.

The net provision for income taxes for the six months ended June 30, 2012 of \$12.8 million consisted of \$10.9 million of federal income tax expense, \$0.5 million of state income tax expense and \$1.4 million of tax expense for our Canadian subsidiary.

Our effective tax rate for the six months ended June 30, 2013 was 16.2% compared with 35.9% for the six months ended June 30, 2012.

Included in our tax expense for our U.S. subsidiaries for the six months ended June 30, 2012 was income tax provision of \$10.4 million on the gain recorded in conjunction with the contribution of the net assets of Chrome for the investment in Chrome Data Solutions, \$1.2 million of expense from the elimination of the Chrome deferred tax assets and goodwill, income tax provision of \$2.0 million on the gain recorded from the sale of a Chrome-branded asset, \$0.2 million of a reduction in valuation allowance resulting from the asset sale, and \$0.4 million of benefit on the change in value of our warrant in TrueCar, which combined resulted in a 40.9% impact to the rate.

Liquidity and Capital Resources

We expect that our liquidity requirements will continue to be primarily for working capital, acquisitions, capital expenditures and general corporate purposes. Our capital expenditures, software and website development costs for the six months ended June 30, 2013 were \$29.3 million, of which \$23.5 million was paid in cash.

As of June 30, 2013, we had \$121.6 million of cash and cash equivalents, \$43.8 million in short-term marketable securities and \$180.0 million in working capital, as compared to \$143.8 million of cash and cash equivalents, \$34.0 million in short-term marketable securities, \$4.4 million in long-term marketable securities and \$172.1 million in working capital as of December 31, 2012.

On April 1, 2013, we acquired the nets assets of Casey & Casey for \$21.3 million in cash. For further information, please refer to Note 11 in the accompanying notes to the consolidated financial statements included in this Quarterly Report on Form 10-Q.

In July 2013, a payment of \$12.4 million was made relating to interest and maturity of the note in connection with the purchase of eCarList, LLC in July 2011.

We expect to have sufficient liquidity to meet our short-term liquidity requirements (including capital expenditures and acquisitions) through working capital and net cash flows from operations, cash on hand, investments in marketable securities and our credit facility.

The following table sets forth the cash flow components for the following periods (in thousands):

	Six Months Ended	
	June 30,	
	2013	2012
Net cash provided by operating activities	\$20,508	\$26,550
Net cash used in investing activities	\$(50,378)	\$(75,488)
Net cash provided by financing activities	\$8,737	\$186,449

Operating Activities

The decrease in net cash provided by operations of \$6.0 million is primarily due to a reduction in net income of \$19.1 million and non-cash items including a decrease in deferred tax provision of \$12.0 million, offset by a \$33.2 million gain recorded from the contribution of net assets of Chrome for our investment in Chrome Data Solutions during 2012, an increase in depreciation and amortization of \$3.9 million, additional amortization of debt issuances costs and debt discount of \$1.7 million and additional earnings from equity method investments of \$2.2 million. Also contributing to the increase were net changes in operating assets and liabilities of \$13.3 million, primarily in accounts receivable.

The decrease of \$12.0 million in deferred tax provision was a result of the \$0.6 million deferred tax benefit for the three months ending June 30, 2013 as compared to a deferred tax provision of \$11.4 million for the six months ending June 30, 2012. The 2012 deferred tax provision of \$11.4 million includes \$10.4 million of deferred tax expense on the gain from the contribution of the net assets of Chrome and \$1.2 million of deferred tax expense from the elimination of Chrome net deferred tax assets.

Investing Activities

The decrease in net cash used in investing activities of \$25.1 million is primarily the result of a decrease in purchases of marketable securities of \$42.9 million and an increase in sales and maturities of marketable securities of \$16.8 million. These increases were offset by an increase in capital expenditures, software and website development costs of \$9.9 million, \$5.5 million of proceeds from the sale of a Chrome branded asset in 2012, the acquisition, net of cash acquired, of Casey & Casey of \$21.0 million, and \$1.8 million of cash which was included in the contribution of the net assets of Chrome to the Chrome Data Solutions joint venture in the six months ended June 30, 2012.

Financing Activities

The decrease in net cash provided by financing activities of \$177.7 million is due to the March 2012 issuance of our senior convertible notes of \$200.0 million, net payment for the call spread overlay of \$14.2 million, and \$7.7 million of debt issuance costs from fees paid for the senior convertible notes and the amended credit facility, offset by an decrease of \$0.4 million of principal payments on capital lease obligations and financing arrangements.

Contractual Obligations

As of June 30, 2013, there were no material changes in our contractual obligations as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2012.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements or relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which are typically established for the purpose of facilitating off-balance sheet arrangements or for other contractually narrow or limited purposes.

Industry Trends

We are impacted by trends in both the automotive retail industry and the credit finance markets. Our financial results are impacted by the number of dealers serviced and the number of vehicles sold. The number of transactions processed through our network is impacted by the level of indirect financing and leasing by our participating lender customers, special promotions by automobile manufacturers and the level of indirect financing and leasing by captive finance companies not available in our network.

The industry has been impacted by a variety of market disruptions. The number of franchise dealerships declined by approximately 2,300, or 11%, between 2008 and 2010 as a result of the general economic environment and the bankruptcy and emergence of two major automobile manufacturers. In recent years, the franchise dealership count has remained consistent at approximately 17,500 based on data from the National Automobile Dealers Association. We do not anticipate a significant change in the number of franchise dealerships over the next few years. A reduction in the number of automotive dealers reduces our opportunities to sell our subscription products.

The number of vehicles sold by dealerships participating on our networks has grown each of the last three years, as the economic environment has recovered. Sales of new vehicles have grown an average of 11% annually over this period, based on data from Automotive News. At this rate of growth, annual new vehicles sales will reach pre-recession (prior to 2007) volume in 2014. The supply of used vehicles that are newer models is limited compared to pre-recession levels due to the decline in new car sales, fleet purchases and leasing during the recession. The total used vehicle supply will likely not increase until at least 2015 as the more recent increases in new vehicles sold start to be traded in to dealerships or leases are returned. In addition, while total supply remains consistent, the used car market mix expects to continue to change with a larger percentage of used vehicles being sold by franchised and independent dealers, and less through private sales.

The number of lending relationships between the various lenders and dealers available through our network continues to increase as the number of dealers has stabilized and lenders are deploying more capital to auto finance. Reduced dealer rooftops and strengthening annual sales rates have resulted in a general increase in profitability for dealers for the past few years. While increased profitability may be expected to increase the number of subscriptions, the dealers need for solutions may not be as high as they were during more difficult economic periods, in which certain offerings were essential to dealerships for maintaining liquidity.

Purchases of new automobiles are typically discretionary for consumers and have been, and may continue to be, affected by negative trends in the economy, including the cost of energy and gasoline, the availability and cost of credit, increased federal taxation, residential and commercial real estate markets, reductions in business and consumer confidence, stock market volatility and increased unemployment.

Effects of Inflation

Our monetary assets, consisting primarily of cash and cash equivalents, receivables and long-term investments, and our non-monetary assets, consisting primarily of intangible assets and goodwill, are not affected significantly by inflation. We believe that replacement costs of equipment, furniture and leasehold improvements will not materially affect our operations. However, the rate of inflation affects our expenses, which may not be readily recoverable in the prices of products and services we offer.

Item 3. *Quantitative and Qualitative Disclosures about Market Risk*

Interest Rate Exposure

As of June 30, 2013, we had \$121.6 million of cash and cash equivalents and \$43.8 million of short-term marketable securities. As of December 31, 2012, we had \$143.8 million of cash and cash equivalents, \$34.0 million of short-term marketable securities and \$4.4 million of long-term marketable securities. Our investments are subject to interest rate and credit risk. Our general policy of investing in securities with a weighted average maturity of three months or less minimizes our interest and credit risk.

Reductions in interest rates and changes in investments could materially impact our interest income and may impact future operating results. An interest rate fluctuation of 1% would have an effect of approximately \$0.2 million and \$0.4 million on consolidated operating results for the three and six months ended June 30, 2013, respectively.

Senior Convertible Notes

On March 5, 2012, we issued \$200.0 million aggregate principal amount of 1.50% senior convertible notes in a private placement. The fair market value of senior convertible notes is subject to interest rate and market price risk due to the convertible feature of the notes and other factors. Generally the fair market value of fixed interest rate debt will increase as interest rates fall and decrease as interest rates rise. The fair market value of the senior convertible notes may also increase as the market price of our stock rises and decrease as the market price of the stock falls. Interest rate and market value changes affect the fair market value of the senior convertible notes, and may affect the prices at which we would be able to repurchase such notes were we to do so. These changes do not impact our financial position, cash flows or results of operations.

In connection with the offering of the senior convertible notes, we entered into privately negotiated convertible note hedge transactions with the hedge counterparties. The convertible note hedge transactions will cover, subject to customary anti-dilution adjustments, the number of shares of our common stock that will initially underlie the notes and are intended to reduce the potential dilutive impact of the conversion feature of the notes. We have also entered into separate privately negotiated warrant transactions with the hedge counterparties.

The convertible note hedge will terminate upon the earlier of the maturity date of the notes or the first day the notes are no longer outstanding. We paid \$43.9 million for the convertible note hedges, which were recorded as a reduction to additional paid-in capital.

The warrant transactions have an initial strike price of approximately \$46.18 per share, and may be settled in cash or shares of our common stock, at our option. The warrant transactions will have a dilutive effect to the extent that the market price per share of our common stock exceeds the applicable strike price of the warrants. Proceeds received from the warrant transactions totaled \$29.7 million and were recorded as additional paid-in capital. The warrants expire at various dates during 2017.

The convertible note hedge and warrants are both considered indexed to our common stock and classified as equity; therefore, the convertible note hedge and warrants are not accounted for as derivative instruments. Changes in the market value of our common stock impact the fair value of the convertible note hedge and warrants. These changes do not impact our financial position, cash flows or results of operations.

See Note 10 to our consolidated financial statements included in Item 1 of Part I of this report for more information regarding the notes.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

We carried out an evaluation under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. In designing and evaluating our disclosure controls and procedures, we and our management recognize that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and our management necessarily was required to apply its judgment in evaluating and implementing possible controls and procedures. Based upon that evaluation, our chief executive officer and chief financial officer have concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective at this reasonable assurance level to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms; and (ii) accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended June 30, 2013, which were identified in connection with management's evaluation required by paragraph (d) of Rule 13a-15 and 15d-15 under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

We continue to convert our various business information systems to a single SAP ERP system. We are employing a phased implementation approach that will provide continued monitoring and assessment to maintain the effectiveness of internal control over financial reporting during and after the conversions. The conversions were not in response to any identified deficiency or weakness in our internal control over financial reporting.

On April 1, 2013, we acquired the net assets of Casey & Casey. We are in the process of analyzing, evaluating and, where necessary, implementing changes in controls and procedures. As a result, the process may result in additions or changes to our internal control over financial reporting. Casey & Casey will be excluded from management's assessment of internal control over financial reporting as of December 31, 2013.

PART II. OTHER INFORMATION

Item 1. *Legal Proceedings*

From time to time, we are a party to litigation matters arising in connection with the normal course of our business, none of which is expected to have a material adverse effect on us. In addition to the litigation matters arising in connection with the normal course of our business, we are party to the litigation described under Note 15 in the accompanying notes to the consolidated financial statements included in this Quarterly Report on Form 10-Q under the heading “Legal Proceedings” and incorporated by reference herein.

Item 1A. *Risk Factors*

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in the section entitled “Risk Factors” in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2012, which was filed with the SEC on February 26, 2013, that could materially affect our business, financial condition or results of operations. There were no material changes in our risk factors from those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2012, other than as provided below.

We are subject, directly and indirectly, to extensive and complex federal and state regulation and new regulations and/or changes to existing regulations may adversely affect our business.

The indirect automotive financing and automotive retail industries are subject to extensive and complex federal and state regulation.

We are directly and indirectly subject to various laws and regulations. Federal laws and regulations governing privacy and security of consumer information generally apply in the context of our business to our clients, and to us as a service provider, which certain regulations obligate our clients to monitor. These include the Fair Credit Reporting Act (FCRA), the Gramm-Leach-Bliley Act (the GLB Act) and regulations implementing its information safeguarding requirements, the Interagency Guidelines Establishing Information Security Standards, the Interagency Guidance on Response Programs for Unauthorized Access to Customer Information and Customer Notice, the Junk Fax Prevention Act of 2005, the CAN-SPAM Act of 2003, the Telephone Consumer Protection Act, the Dodd–Frank Wall Street Reform and Consumer Protection Act, and applicable Federal Communications Commission (FCC) telemarketing rules, and the Federal Trade Commission’s (FTC) Privacy Rule, Safeguards Rule, Consumer Report Information Disposal Rule, Telemarketing Sales Rule, Risk-Based Pricing Rule, and Red Flags Rule, as well as regulations

promulgated by the Federal Reserve Board and the Consumer Financial Protection Bureau (CFPB). If we, or a lender or dealer discloses or uses consumer information provided through our system in violation of these or other laws or regulations, or engage in other prohibited conduct, we may be subject to claims or enforcement actions by state or federal regulators. We cannot predict whether such claims or enforcement actions will arise or the extent to which, if at all, we may be held liable. Such claims or enforcement actions could have a material adverse effect on our business, prospects, financial condition and results of operations.

A majority of states have passed, or are currently contemplating, consumer protection, privacy, and data security laws or regulations that may relate to our business. The FCRA contains certain provisions that explicitly preempt some state laws to the extent the state laws seek to regulate certain specified areas, including the responsibilities of persons furnishing information to consumer reporting agencies. Unlike the FCRA, however, the GLB Act does not limit the ability of the states to enact privacy legislation that provides greater protections to consumers than those provided by the GLB Act. Some state legislatures or regulatory agencies have imposed, and others may impose, greater restrictions on the disclosure of consumer information than are already contained in the GLB Act and its implementing regulations, the Interagency Guidelines or the FTC's rules. Any such legislation or regulation could adversely impact our ability to provide our customers with the products and services they require and that are necessary to make our products and services attractive to them.

The CFPB has authority to issue new regulations and bring enforcement actions, including regulations prohibiting and enforcement actions redressing unfair, deceptive, and abusive trade practices relating to consumer financial services. The Federal Trade Commission continues to have supervisory and enforcement authority over most franchised dealers, but the CFPB has supervisory and enforcement authority over independent and buy-here-pay-here dealers as well as financial institutions with assets in excess of \$10 billion and other "larger non-depository participants" in the consumer financial services market. Our financing clients such as banks, finance companies and captives will be subject to the substantive regulations published by the CFPB (and franchised dealers will remain subject to parallel rules of the Federal Reserve Board) and many financing clients will be subject to the CFPB's supervisory authority on consumer finance issues if their assets exceed \$10 billion or they are deemed a "larger, non-depository participant" for consumer financial services. It is anticipated that the CFPB may by regulation in 2013 extend its supervisory authority to include auto lenders as "larger participants" in the market for consumer financial services.

The CFPB is conducting supervisory audits of large auto lenders. If the CFPB enters into a consent decree with one or more lenders on disparate impact credit discrimination claims, it could negatively impact the business of the affected lenders, and potentially the business of dealers and other lenders in the consumer indirect auto finance market. This impact on dealers and lenders could result in a reduction of revenue received by us.

On March 21, 2013, the CFPB issued guidance regarding possible Equal Credit Opportunity Act (ECOA) "disparate impact" credit discrimination in indirect auto finance in connection with dealer rate markups. A "disparate impact" can occur when a facially-neutral practice (such as dealer markups of "buy rates" or the selection of lenders to which dealers submit credit applications) result in statistically significant negative rates or terms for protected classes of persons under ECOA. The CFPB recommended that lenders either implement a compliance program to monitor and assess the impact on ECOA protected classes of dealer rate markups or eliminate dealer rate markups and compensate dealers on a flat fee basis instead. It is too early to tell what impact this guidance will have on industry practices or the impact of any changed industry practices on our business and revenues. In the event that any industry practices result in a

decrease in the number of applications being submitted by dealers on our network to lenders on our network, it could have a material adverse effect on our revenues and profitability.

On May 2, 2013, the Wall Street Journal reported that the CFPB had issued subpoenas to U.S. auto lenders over the sale of service contracts and other credit protection products. These aftermarket products are a significant profit center for our dealer customers. Any regulation or restriction placed on the sale of these products could reduce dealer profitability which could have an adverse impact on the dollar amount that dealers spend on our products and services.

If a federal or state government or agency, such as the federal CFPB or FTC, imposes additional legislative and/or regulatory requirements on us or our customers, or prohibits or limits our activities as currently conducted, we may be required to modify or terminate our products and services in a manner which could undermine our attractiveness or availability to dealers and/or lenders doing business in that jurisdiction.

The use of our electronic contracting product by lenders is governed by relatively new laws.

In the United States, the enforceability of electronic transactions is primarily governed by the E-SIGN Act, a federal law enacted in 2000 that largely preempts inconsistent state law, and the Uniform Electronic Transactions Act, a uniform state law that was finalized by the National Conference of Commissioners on Uniform State Laws in 1999 and has now been adopted by nearly every state. Case law has generally upheld the use of electronic signatures in commercial transactions and in consumer transactions where proper notice is provided and the consumer consents to transact business electronically. Uniform Commercial Code (UCC) 9-105 provides requirements to perfect security interests in electronic chattel paper. These laws impact the degree to which the lenders in our network use our electronic contracting product. We believe that our electronic contracting product enables the perfection of a security interest in electronic chattel paper by meeting the “transfer of control” requirements of UCC 9-105. Certain of our financial institution clients have received third-party legal opinions to that effect. However, this issue has not been challenged in any legal proceeding. If a court were to find that our electronic contracting product is not sufficient to perfect a security interest in electronic chattel paper, or if existing laws were to change, our business, prospects, financial condition and results of operations could be materially adversely affected. Federal and state regulatory requirements imposed on our lender customers, such as the SEC’s Regulation AB relating to servicers of asset backed securities, may also result in our incurring additional expenses to facilitate lender compliance regarding the use of our eContracting product.

New legislation or changes in existing legislation may adversely affect our business.

Our ability to conduct, and our cost of conducting, business may be adversely affected by a number of legislative and regulatory proposals concerning aspects of the Internet, which are currently under consideration by federal, state, local and foreign governments, administrative agencies such as the FTC, the CFPB the FCC, and various courts. These proposals include, but are not limited to, the following matters: on-line content, user privacy, taxation, access charges, and so-called “net-neutrality” liability of third-party activities and jurisdiction. Moreover, we do not know how existing laws relating to these or other issues will be applied to the Internet. The adoption of new laws or the application of existing laws could decrease the growth in the use of the Internet, which could in turn decrease the demand for our

products and services, increase our cost of doing business or otherwise have a material adverse effect on our business, prospects, financial condition and results of operations. Furthermore, government restrictions on Internet content or anti-“net neutrality” legislation could slow the growth of Internet use and decrease acceptance of the Internet as a communications and commercial medium and thereby have a material adverse effect on our business, prospects, financial condition and results of operations.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Purchases of Equity Securities by the Issuer

From time to time, in connection with the vesting of restricted common stock units under our incentive award plans, we have received shares of our common stock in consideration of the tax withholdings due upon the vesting of restricted common stock units.

The following table sets forth the repurchases for the three months ended June 30, 2013, all of which were in conjunction with the vesting of restricted common stock units:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Program	Maximum Number of Shares That May Yet be Purchased Under the Program
April 2013	—	\$ —	n/a	n/a
May 2013	2,681	\$ 31.27	n/a	n/a
June 2013	—	\$ —	n/a	n/a
Total	2,681			

Item 3. *Defaults Upon Senior Securities*

None.

Item 4. *Mine Safety Disclosures*

Not applicable.

Item 5. *Other Information*

None.

Item 6. *Exhibits*

See the Exhibit Index following the signature page to this Quarterly Report on Form 10-Q for the information required by this item.

35

SIGNATURE

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

Dealertrack Technologies, Inc.

August 6, 2013 /s/ Eric D. Jacobs

Eric D. Jacobs

Executive Vice President, Chief Financial and Administrative Officer

(Duly Authorized Officer and Principal Financial Officer)

EXHIBIT INDEX

Exhibit

Number Description of Document

- 31.1 Certification of Mark F. O'Neil, Chairman, President and Chief Executive Officer, pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Eric D. Jacobs, Executive Vice President, Chief Financial and Administrative Officer, pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certifications of Mark F. O'Neil, Chairman, President and Chief Executive Officer, and Eric D. Jacobs, Executive Vice President, Chief Financial and Administrative Officer, pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.