

DST SYSTEMS INC
Form 10-Q
November 08, 2010
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2010

or

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

For the transition period from _____ **to** _____

Commission File Number 1-14036

DST SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

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Delaware

(State or other jurisdiction of
incorporation or organization)

43-1581814

(I.R.S. Employer
Identification No.)

333 West 11th Street, Kansas City, Missouri

(Address of principal executive offices)

64105

(Zip Code)

(816) 435-1000

(Registrant's telephone number, including area code)

No Changes

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer
(do not check if a smaller reporting company)

Smaller reporting company

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

Number of shares outstanding of the Company's common stock as of October 31, 2010:

Common Stock \$0.01 par value 46,247,069

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DST Systems, Inc.

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September 30, 2010

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DST Systems, Inc.

Form 10-Q

September 30, 2010

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Introductory Comments

The Condensed Consolidated Financial Statements of DST Systems, Inc. ("DST" or the "Company") included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the United States Securities and Exchange Commission. Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to enable a reasonable understanding of the information presented. These Condensed Consolidated Financial Statements should be read in conjunction with the Company's audited financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009.

The results of operations for the three and nine months ended September 30, 2010 are not necessarily indicative of the results to be expected for the full year 2010.

Table of Contents**DST Systems, Inc.****Condensed Consolidated Balance Sheet***(in millions, except per share amounts)**(unaudited)*

	September 30, 2010	December 31, 2009
ASSETS		
Current assets		
Cash and cash equivalents	\$ 75.3	\$ 106.2
Funds held on behalf of clients	289.8	208.3
Client funding receivable	61.1	103.8
Accounts receivable	301.0	167.2
Deferred income taxes	19.2	19.2
Other assets	45.3	74.2
	791.7	678.9
Investments	1,371.6	1,411.8
Properties	539.5	536.3
Goodwill	222.5	183.6
Intangible assets	51.0	43.0
Other assets	55.9	59.2
Total assets	\$ 3,032.2	\$ 2,912.8
LIABILITIES AND EQUITY		
Current liabilities		
Current portion of debt	\$ 256.4	\$ 658.1
Client funds obligations	350.9	312.1
Accounts payable	67.0	69.9
Accrued compensation and benefits	102.5	90.8
Deferred revenues and gains	45.6	59.1
Other liabilities	86.7	91.2
	909.1	1,281.2
Long-term debt	1,005.1	563.8
Income taxes payable	55.3	57.1
Deferred income taxes	291.6	312.0
Other liabilities	79.6	64.3
Total liabilities	2,340.7	2,278.4
Commitments and contingencies (Note 9)		
Equity		
DST Systems, Inc stockholders' equity		
Common stock, \$0.01 par; 400 million shares authorized, 95.3 million shares issued	1.0	1.0
Additional paid-in capital	246.9	235.6
Retained earnings	2,960.5	2,749.6
Treasury stock (49.1 million and 46.2 million shares, respectively), at cost	(2,818.6)	(2,704.3)
Accumulated other comprehensive income	280.9	352.5
Total DST Systems, Inc. stockholders' equity	670.7	634.4
Non-controlling interest	20.8	

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Total equity		691.5		634.4
Total liabilities and equity	\$	3,032.2	\$	2,912.8

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

Table of Contents**DST Systems, Inc.****Condensed Consolidated Statement of Income***(in millions, except per share amounts)**(unaudited)*

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Operating revenues	\$ 419.0	\$ 395.6	\$ 1,294.0	\$ 1,195.7
Out-of-pocket reimbursements	148.2	156.1	453.8	470.9
Total revenues	567.2	551.7	1,747.8	1,666.6
Costs and expenses	459.3	454.6	1,363.4	1,367.3
Depreciation and amortization	33.5	34.5	99.4	93.8
Income from operations	74.4	62.6	285.0	205.5
Interest expense	(12.1)	(8.8)	(33.7)	(28.9)
Other income, net	9.4	33.2	67.8	60.6
Equity in earnings of unconsolidated affiliates	8.9	7.8	27.0	24.0
Income before income taxes and non-controlling interest	80.6	94.8	346.1	261.2
Income taxes	26.4	33.9	121.0	78.4
Net income	54.2	60.9	225.1	182.8
Non-controlling interest	0.1		0.1	
Net income attributable to DST Systems, Inc.	\$ 54.3	\$ 60.9	\$ 225.2	\$ 182.8
Average common shares outstanding	46.6	49.7	47.2	49.7
Average diluted shares outstanding	46.9	50.2	47.5	50.0
Basic earnings per share	\$ 1.17	\$ 1.22	\$ 4.77	\$ 3.68
Diluted earnings per share	\$ 1.16	\$ 1.21	\$ 4.74	\$ 3.65
Cash dividends per share of common stock	\$	\$	\$ 0.30	\$

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

Table of Contents**DST Systems, Inc.****Condensed Consolidated Statement of Cash Flows***(in millions)**(unaudited)*

	Nine Months Ended September 30,	
	2010	2009
Cash flows operating activities:		
Net income	\$ 225.1	\$ 182.8
Depreciation and amortization	99.4	93.8
Net (gains) losses on investments	(41.4)	4.8
Net (gain) loss on the extinguishment of senior convertible debentures	1.0	(5.9)
Gain on equity interest in Argus Health Systems, Inc.		(41.7)
Amortization of share based compensation	15.0	21.2
Equity in earnings of unconsolidated affiliates	(27.0)	(24.0)
Dividends from unconsolidated affiliates	2.5	29.3
Deferred income taxes	16.1	25.7
Changes in accounts receivable	(117.1)	56.7
Proceeds from accounts receivable securitization program, net		10.0
Changes in accounts payable and accrued liabilities	10.4	(25.8)
Changes in income taxes payable	16.3	(41.0)
Other, net	11.4	3.1
Total adjustments to net income	(13.4)	106.2
Net	211.7	289.0
Cash flows investing activities:		
Capital expenditures	(74.8)	(70.2)
Proceeds from unconsolidated affiliates	10.5	1.0
Investments in securities	(169.1)	(72.3)
Proceeds from sales/maturities of investments	149.5	102.1
Net (increase) decrease in restricted cash and cash equivalents held to satisfy client funds obligations	(81.5)	132.7
Acquisition of businesses, net of cash acquired	(6.3)	
Acquisition of interest in Argus Health Systems, Inc., net of cash acquired		(47.8)
Other, net	0.5	0.3
Net	(171.2)	45.8
Cash flows financing activities:		
Proceeds from issuance of common stock	10.6	7.1
Principal payments on debt	(27.8)	(11.2)
Repurchases of senior convertible debentures	(443.6)	(131.3)
Net proceeds from issuance of senior notes	370.0	
Net proceeds from accounts receivable securitization program	125.0	
Net increase (decrease) in client funds obligations	81.5	(144.2)
Net borrowings on revolving credit facilities	(35.0)	(30.1)
Payment of debt issuance costs	(8.2)	
Common stock repurchased	(129.9)	(7.6)
Payment of cash dividends	(14.3)	
Excess tax benefits from share based compensation	0.3	
Net	(71.4)	(317.3)
Net (decrease) increase in cash and cash equivalents	(30.9)	17.5

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Cash and cash equivalents, beginning of period		106.2		78.7
Cash and cash equivalents, end of period	\$	75.3	\$	96.2

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

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DST Systems, Inc.

Notes to Condensed Consolidated Financial Statements

(unaudited)

1. Summary of Accounting Policies

The Condensed Consolidated Financial Statements of DST Systems, Inc. ("DST" or the "Company") included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the United States Securities and Exchange Commission ("SEC"). Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to enable a reasonable understanding of the information presented. The Condensed Consolidated Balance Sheet as of December 31, 2009 has been derived from the audited Consolidated Balance Sheet at that date, but does not include all of the information and notes required by GAAP for complete financial statements. These Condensed Consolidated Financial Statements should be read in conjunction with the Company's audited financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009.

In the opinion of management, the accompanying unaudited Condensed Consolidated Financial Statements contain all adjustments (consisting of normal interim closing procedures) necessary to present fairly the consolidated financial position of the Company and its subsidiaries at September 30, 2010, and the results of operations for the three and nine months ended September 30, 2010 and 2009, and cash flows for the nine months ended September 30, 2010 and 2009.

The results of operations for the three and nine months ended September 30, 2010 are not necessarily indicative of the results to be expected for the full year 2010.

2. Business Combination

dsicmm Group Limited

On July 30, 2010, DST, through its wholly-owned U.K. subsidiary, Innovative Output Solutions Limited ("IOS"), acquired dsicmm Group Limited ("dsicmm") for cash and the issuance of IOS stock. Prior to closing the transaction, IOS held DST's debt-free U.K. print/mail operations. After completion of the transaction, DST will own approximately 70.5% of IOS and the remaining 29.5% will be owned by a group of the former stockholders of dsicmm. DST has consolidated the financial results of the combined IOS business from the closing date and has reflected the 29.5% owned by former stockholders of dsicmm as a non-controlling interest.

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dsicmm provides integrated print and communication solutions in the U.K. dsicmm has approximately 1,200 employees and recorded operating revenues post acquisition of approximately \$22.0 million and a loss from operations of \$2.9 million during the two months ended September 30, 2010. DST believes that the acquisition of dsicmm complements its existing Output Solutions business in the U.K., increases the overall size of the business, broadens the service/product offerings and expands and diversifies the client base.

The Company has not yet finalized its accounting for the acquired assets of dsicmm; when finalized, it is possible that amounts appearing in the table below of net assets acquired will be adjusted. DST has preliminarily recognized identifiable intangible assets (comprised of customer relationships of \$11.0 million and proprietary software of \$7.9 million) and goodwill of \$34.6 million, resulting from the acquisition. DST estimates annual amortization for acquired dsicmm intangible assets will be approximately \$3.3 million. Goodwill of \$34.6 million from the acquisition is comprised of the assembled workforce of dsicmm and other assets and is included in the Output Solutions Segment. None of the goodwill is expected to be deductible for income tax purposes.

Assuming the acquisition of dsicmm Group Limited had occurred January 1, 2009, the Company's total revenues would have been approximately \$1,837.6 million and \$1,772.7 million for the nine months ended September 30, 2010 and 2009, respectively. Consolidated proforma net income and diluted earnings per share would not have

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been materially different from the reported amounts for the nine months ended September 30, 2010 and 2009. The unaudited proforma amounts are not indicative of what actual consolidated results of operations might have been if the acquisition had been effective at the beginning of 2009.

The following table summarizes the consideration for dsicmm and the preliminary allocation of the fair value of dsicmm to the fair values of assets acquired and liabilities assumed at July 30, 2010 (in millions).

Consideration	
Cash paid	\$ 4.6
Fair value of shares issued of Innovative Output Solutions Limited (non monetary)	21.2
Fair value of dsicmm Group Limited	\$ 25.8
Recognized amounts of identifiable assets acquired and liabilities assumed	
Accounts receivable	\$ 25.7
Other current assets	7.3
Investments	0.4
Properties (includes \$7.9 million of proprietary software)	39.0
Intangible assets	11.0
Goodwill	34.6
Total assets	118.0
Other current liabilities	26.7
Income tax liabilities	1.8
Long-term debt	51.4
Deferred income tax liabilities	7.2
Non-current liabilities	5.1
Total liabilities	92.2
Net assets acquired	\$ 25.8

As a result of the acquisition of dsicmm, the Company's IOS subsidiary has a non-controlling investor as follows:

Non-controlling interest at December 31, 2009	\$
Exchange of non-controlling interest in IOS for a controlling interest in dsicmm	20.9
Net loss attributable to non-controlling interest during 2010	(0.1)
Non-controlling interest at September 30, 2010	\$ 20.8

Table of Contents**3. Investments**

Investments are as follows (in millions):

	2010 Ownership Percentage	Carrying Value	
		September 30, 2010	December 31, 2009
Available-for-sale securities:			
State Street Corporation	2%	\$ 398.5	\$ 460.7
Computershare Ltd.	3%	165.0	228.8
Euronet Worldwide	4%	33.9	41.4
Other available-for-sale securities		208.9	162.4
		806.3	893.3
Unconsolidated affiliates:			
Boston Financial Data Services, Inc.	50%	166.2	154.5
International Financial Data Services, U.K.	50%	73.1	65.1
International Financial Data Services, L.P.	50%	44.0	38.5
Unconsolidated real estate affiliates		72.3	88.0
Other unconsolidated affiliates		13.0	13.4
		368.6	359.5
Other:			
Trading securities		49.5	48.8
Held-to-maturity		9.5	6.9
Investments, at cost		137.7	103.3
		196.7	159.0
Total investments		\$ 1,371.6	\$ 1,411.8

Certain information related to the Company's available-for-sale securities is as follows (in millions):

	September 30, 2010	December 31, 2009
Book cost basis	\$ 341.6	\$ 319.4
Gross unrealized gains	446.9	557.8
Gross unrealized losses	(3.0)	(0.9)
Unrealized gain from changes in foreign currency exchange rates	20.8	17.0
Market value	\$ 806.3	\$ 893.3

During the nine months ended September 30, 2010 and 2009, the Company received \$146.8 million and \$95.2 million, respectively, from the sale of investments in available-for-sale securities. Gross realized gains of \$2.4 million and \$22.8 million and gross realized losses of \$1.2 million and \$0.3 million, respectively, were recorded during the three months ended September 30, 2010 and 2009 from available-for-sale securities. Gross realized gains of \$44.1 million and \$28.3 million and gross realized losses of \$2.3 million and \$2.4 million, respectively, were recorded during the nine months ended September 30, 2010 and 2009 from available-for-sale securities. In addition, the Company recorded unrealized losses on available-for-sale securities of \$0.3 million and \$0.7 million for the three and nine months ended September 30, 2010 compared to \$26.8 million for the nine months ended September 30, 2009, related to other than temporary investment impairments. There were no investment impairments on available-for-sale securities for the three months ended September 30, 2009. Included in the proceeds received from the sale of investments in available-for-sale securities for the nine months ended September 30, 2010 is \$52.4 million of proceeds resulting

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from the sale of 4.8 million shares of Computershare Ltd., which resulted in a gain of \$28.8 million.

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The following table summarizes the fair value and gross unrealized losses of the Company's investments by the length of time that the securities have been in a continuous loss position, at September 30, 2010 (in millions):

	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Common stock	\$ 31.8	\$ 3.0	\$	\$	\$ 31.8	\$ 3.0

In addition to recording other than temporary investment impairments on available-for-sale securities, the Company records lower of cost or market valuation adjustments on private equity fund investments and other cost method investments when impairment conditions are present. There were no impairments on private equity and other investments for the three months ended September 30, 2010. During the nine months ended September 30, 2010, the Company recorded \$0.8 million of impairments on private equity and other investments compared to the three and nine months ended September 30, 2009 when the Company recorded impairments of \$0.2 million and \$4.4 million. The impairments recorded related primarily to investments in the Financial Services Segment and the Investments and Other Segment. A decline in a security's net realizable value that is other than temporary is treated as a loss based on quoted or derived market value and is reflected in Other Income, net in the Condensed Consolidated Statement of Income.

Future adverse changes in market conditions or poor operating results of underlying investments could result in losses or an inability to recover the carrying value of the investments that may not be reflected in an investment's current carrying value, thereby possibly requiring an impairment charge in the future. Such a charge could have a material effect on the Company's financial position.

Equity in earnings (losses) of unconsolidated affiliates, net of income taxes provided by the unconsolidated affiliates follows (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
BFDS	\$ 4.0	\$ 2.2	\$ 11.7	\$ 9.0
IFDS, U.K.	3.1	2.0	9.6	5.8
IFDS, L.P.	1.5	2.1	5.5	4.7
Argus				(1.5)
Other	0.3	1.5	0.2	6.0
	\$ 8.9	\$ 7.8	\$ 27.0	\$ 24.0

DST acquired the remaining 50% equity interest in Argus Health Systems, Inc. (Argus) on March 31, 2009 and no longer records equity in earnings of Argus, but rather consolidates the Argus results in DST's financial statements.

The Company is a limited partner in various private equity funds. At September 30, 2010 and December 31, 2009, the Company's carrying value of these private equity fund investments was approximately \$131.2 million and \$94.4 million, respectively. At September 30, 2010, the Company had future capital commitments related to these private equity fund investments of approximately \$104.4 million.

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Authoritative accounting guidance on fair value measurements establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

As of September 30, 2010 and December 31, 2009, the Company held certain investment assets that are required to be measured at fair value on a recurring basis. These investments include the Company's available-for-sale equity securities and trading securities whereby fair value is determined using quoted prices in active markets. Accordingly, the fair value measurements of these investments have been classified as Level 1 in the table below. Included in funds held on behalf of clients at September 30, 2010 and December 31, 2009 are approximately \$22.3 million and \$11.1 million, respectively, of available-for-sale fixed income securities held to satisfy client funds obligations. In addition, the Company has interest rate swaps that are required to be reported at fair value. Fair value for the available-for-sale fixed income securities and for the interest rate swaps was determined using inputs from quoted prices for similar assets and liabilities in active markets and other observable inputs directly or indirectly. Accordingly, these investments have been classified as Level 2 in the table below.

The following table presents assets and liabilities measured at fair value on a recurring basis (in millions):

	Fair Value Measurements at Reporting Date Using			
	September 30, 2010	Quoted prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Equity securities	\$ 819.6	\$ 819.6	\$	\$
Fixed income securities	58.5		58.5	
Interest rate swap liabilities	(6.4)		(6.4)	
Total	\$ 871.7	\$ 819.6	\$ 52.1	\$

	Fair Value Measurements at Reporting Date Using			
	December 31, 2009	Quoted prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Equity securities	\$ 937.7	\$ 937.7	\$	\$
Fixed income securities	15.5		15.5	
Interest rate swap liability	(1.9)		(1.9)	

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Total	\$	951.3	\$	937.7	\$	13.6	\$
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At September 30, 2010 and December 31, 2009, one of DST's unconsolidated affiliates had an interest rate swap with a fair market value liability of \$67.5 million and \$35.6 million, respectively. The unconsolidated affiliate used inputs from quoted prices for similar assets and liabilities in active markets and other observable inputs directly or indirectly related to the measurement of the interest rate swap. The fair value measurement of the interest rate swap has been classified as Level 2 by the unconsolidated affiliate. The above table presents only assets and liabilities measured at fair value for which the Company controls, and accordingly excludes items held by unconsolidated affiliates.

5. Goodwill and Intangible Assets

Goodwill

The following table summarizes the changes in the carrying amount of goodwill for the nine months ended September 30, 2010, by Segment (in millions):

	December 31, 2009		Acquisitions	Disposals	Other	September 30, 2010	
Financial Services	\$	174.9	\$	\$	\$	3.1	\$ 178.0
Output Solutions		8.7		35.8			44.5
Total	\$	183.6	\$	35.8	\$	3.1	\$ 222.5

Intangible Assets

The following table summarizes intangible assets (in millions):

	September 30, 2010		December 31, 2009	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortizable intangible assets:				
Customer relationships	\$ 63.4	\$ 15.1	\$ 51.2	\$ 11.6
Other	6.0	3.3	6.0	2.6
Total	\$ 69.4	\$ 18.4	\$ 57.2	\$ 14.2

As described in Note 2, the acquisition of dsicmm on July 30, 2010 resulted in \$34.6 million of goodwill and \$11.0 million in customer relationship intangible assets. These items are not deductible for income tax purposes.

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Amortization of intangible assets for the three and nine months ended September 30, 2010 was approximately \$1.7 million and \$4.2 million compared to \$1.2 million and \$3.2 million for the three and nine months ended September 30, 2009. Annual amortization for intangible assets recorded as of September 30, 2010 is estimated to be \$1.4 million for the remainder of 2010, \$5.5 million for 2011, \$5.2 million for 2012, \$4.6 million for 2013, \$4.5 million for 2014 and \$29.8 million thereafter.

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The Company is obligated under notes and other indebtedness as follows (in millions):

	September 30, 2010	December 31, 2009
Accounts receivable securitization program	\$ 125.0	\$ 8.9
Secured promissory notes	4.4	8.8
Equipment credit facilities	7.6	111.6
Real estate credit agreement	109.3	151.8
Convertible senior debentures		171.3
Series A		257.0
Series B		356.2
Series C	143.6	416.3
Revolving credit facilities	370.0	100.0
Senior notes	100.0	75.0
Related party promissory note	45.4	21.2
Other indebtedness	1,261.5	1,221.9
Less current portion of debt	256.4	658.1
Long-term debt	\$ 1,005.1	\$ 563.8

Accounts Receivable Securitization Program

On January 1, 2010, the Company adopted new authoritative accounting guidance related to transfers of financial assets. This guidance changed the accounting for securitizations of mortgages and other financial instruments and the consolidation requirements for qualifying special-purpose entities (QSPE). Besides removing the concept of a QSPE, this new accounting guidance: a) clarified the determination of whether a transferor and all the entities included in the transferor's financial statements being presented have surrendered control over transferred financial assets; b) defined the term participating interest to establish specific conditions for reporting a transfer of a portion of a financial asset as a sale; c) required a transferor to recognize and initially measure at fair value all assets obtained and liabilities incurred as a result of a transfer of financial assets accounted for as a sale; and d) enhanced disclosures to provide financial statement users with greater transparency about transfers of financial assets and a transferor's continuing involvement with transferred financial assets.

Prior to the adoption of this new authoritative accounting guidance on January 1, 2010, the periodic transfers by the SPE of undivided interests in accounts receivable to the third-party, multi-seller, asset-backed commercial paper conduit met the requirements for sale accounting treatment and were considered an off-balance sheet arrangement. After January 1, 2010, the periodic transfers of undivided interests in accounts receivable no longer qualify for sale accounting treatment in accordance with the new accounting guidance and are accounted for as secured borrowings. DST has continuing involvement with the transferred assets because it maintains servicing responsibilities for the accounts receivable assets included in the accounts receivable securitization program. Accounts receivable assets transferred from DST and certain of its domestic subsidiaries to its wholly-owned, bankruptcy remote special purpose subsidiary contain restrictions because they are not available to satisfy the creditors of any other person, including DST or any of its subsidiaries or affiliates.

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At September 30, 2010, the outstanding amount of undivided interests in the receivables held by the conduit was \$125.0 million, unchanged from December 31, 2009. During the nine months ended September 30, 2010, the Company's accounts receivable increased by \$125.0 million resulting in a cash outflow being reported in the operating section of the cash flow statement and the current portion of debt associated with the accounts receivable securitization program increased by \$125.0 million resulting in a cash inflow being reported in the

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financing section of the cash flow statement. During the nine months ended September 30, 2010, total proceeds from the accounts receivable securitization program were approximately \$625.0 million and total repayments were approximately \$500.0 million which comprises the net cash inflow in the financing section of the statement of cash flows. Costs associated with the accounts receivable securitization program were included in other income during 2009, but are included in interest expense effective January 1, 2010.

On May 20, 2010, the Company renewed the accounts receivable securitization program. In connection with the renewal, the maximum size of the program decreased from \$175 million to \$150 million and the expiration date for the conduit's purchase commitment was changed to May 19, 2011.

Aggregate transfers of undivided interests in the receivables from the SPE to the conduit were \$1,319.3 million and \$1,306.4 million for the nine months ended September 30, 2010 and 2009, respectively.

Equipment credit facilities

The draw period under the Company's existing \$50 million equipment credit facility expired on June 30, 2010. The maturity date for each loan drawn under that facility is the earlier of approximately three years from the initial draw or August 1, 2013.

On June 30, 2010, the Company entered into a new \$50.0 million unsecured credit facility with the same vendor. Proceeds from loans made under the new credit facility can be used to make purchases of the vendor's eligible equipment, software or services. Loans under this credit facility must be made prior to December 31, 2012, the draw period termination date. The maturity date for each loan under this credit facility is the earlier of i) the last day of the thirty first (31st) calendar month following the loan date or ii) June 30, 2015. Interest rates applicable to the loans under this credit facility are generally based on the LIBOR rate plus an applicable margin of 1.5% to 2.5%. The applicable margin is based on a grid schedule that adjusts borrowing costs up or down based upon the Company's consolidated leverage ratio. No amounts were drawn under this facility at September 30, 2010.

Convertible senior debentures

During the three and nine months ended September 30, 2010, the Company recorded a loss of \$1.1 million and \$1.0 million associated with the repurchase of a portion of the Company's senior convertible debentures at a premium to carrying value. The Company repurchased \$67.7 million of the original Series A senior convertible debentures, \$8.8 million of the Series B convertible debentures and \$113.4 million in principal of the original Series C senior convertible debentures during the nine months ended September 30, 2010. During the three and nine months ended September 30, 2009, the Company recorded a gain of \$0.1 million and \$5.9 million associated with the repurchase of a portion of the Company's senior convertible debentures at a discount to carrying value.

In August 2010, the Company had \$9.9 million Series A senior convertible debentures that were put to the Company by debenture holders and redeemed. In September 2010, the entire remaining balance of Series A (\$74.2 million) and Series B (\$168.5 million, which includes \$6.0 million of accreted interest) senior convertible debentures were redeemed, which fully retired these series of debentures. At September 30,

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2010, the Company had approximately \$143.6 million Series C senior convertible debentures outstanding. Beginning August 15, 2013, the Company may redeem for cash all or part of the Series C senior convertible debentures.

Revolving credit facilities

On April 16, 2010, the Company entered into a new syndicated line of credit facility to replace its syndicated revolving line of credit facility that matured on July 1, 2010. The new credit agreement provides for a revolving unsecured credit facility in an aggregate principal amount of up to \$600 million. The interest rates applicable to loans under the new credit agreement are generally based on LIBOR, Federal Funds or prime rates plus applicable margins as defined in the agreement. The revolving credit facility contains grid schedules that adjust borrowing costs up or down based upon the Company's consolidated leverage ratio. The grid schedules may result in fluctuations in borrowing costs ranging from 1.75% to 2.375% over LIBOR and 0.75% to 1.375% over base rate as defined. Additionally, an annual facility fee of 0.25% to 0.625% is required on this revolving syndicated line

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of credit. The credit agreement contains customary restrictive covenants, as well as certain customary events of default. Among other provisions, the credit agreement limits consolidated indebtedness, liens, investments, subsidiary indebtedness, asset dispositions and restricted payments (including stock repurchases and cash dividends), and requires certain leverage and interest coverage ratios to be maintained. If any event of default occurs and is continuing, all amounts payable under the credit agreement may be declared immediately due and payable. The maturity date for the new credit facility is July 1, 2013. On April 16, 2010, the date of the refinancing transaction, the administrative agent transferred \$443.4 million of the outstanding balance under the old credit facility to the new credit facility.

Senior notes

On August 9, 2010, the Company issued \$370.0 million of aggregate principal of privately placed senior notes (collectively, the Senior Notes). The Senior Notes are comprised of \$40 million of 4.19% Series A Senior Notes due August 9, 2015, \$105 million of 4.86% Series B Senior Notes due August 9, 2017, \$65 million of 5.06% Series C Senior Notes due August 9, 2018 and \$160 million of 5.42% Series D Senior Notes due August 9, 2020.

The Senior Notes are unsecured senior obligations of the Company and were issued pursuant to a note purchase agreement dated August 9, 2010 (the Agreement). Interest on the Senior Notes is payable semiannually on February 9 and August 9 of each year, commencing February 9, 2011. The Company may prepay the Notes at any time, in an amount not less than 10% of the aggregate principal amount of the Senior Notes then outstanding, at a price equal to 100% of the principal amount being prepaid, plus accrued and unpaid interest and a make-whole prepayment premium. The Company may be required to prepay all or a portion of the Senior Notes upon the occurrence of any Change in Control , as defined in the Agreement.

Pursuant to the Agreement, any subsidiary of the Company that is required to become a party to or otherwise guarantee the syndicated line of credit facility or other indebtedness in excess of \$100.0 million, will be required to guarantee the Company's obligations under the Senior Notes. The Agreement contains customary restrictive covenants, as well as certain customary events of default, including cross-default provisions. Among other provisions, the Agreement limits the ability of the Company to incur or create liens, sell assets, issue priority indebtedness and change lines of business. The agreement also requires certain leverage and interest coverage ratios to be maintained.

Related party promissory note

On October 27, 2010, the Company amended and restated its related party promissory note with Boston Financial Data Services, Inc. (BFDS). The agreement provides for unsecured revolving borrowings by the Company of up to \$140 million and matures on July 1, 2013. Prior to this amendment, the maximum borrowings under this promissory note was \$100.0 million. From time to time, BFDS may, subject to a ten day notice period, demand a prepayment of the loan by the Company in an amount not to exceed \$25 million in each instance. The interest rate applicable to the loan is based on LIBOR plus an applicable margin correlating to the applicable margin under the Company's \$600 million syndicated line of credit facility. The loan agreement incorporates by reference and requires the Company to comply with the affirmative and negative covenants contained in the Company's \$600 million syndicated line of credit facility.

Other indebtedness

Other indebtedness is primarily comprised of debt obligations that the Company assumed in connection with a business acquisition in 2006 and from the acquisition of dsicmm. The Company assumed aggregate indebtedness of \$51.4 million upon the acquisition of dsicmm. At September 30, 2010, the amount outstanding for debt obligations related to the 2006 business acquisition and the dsicmm acquisition was \$19.5 million and \$25.9 million, respectively.

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Future principal payments of indebtedness at September 30, 2010 are as follows (in millions):

2011	\$	256.4
2012		15.1
2013		364.3
2014		247.3
2015		43.9
Thereafter		334.5
Total	\$	1,261.5

7. Income Taxes

The Company records income tax expense during interim periods based on its best estimate of the full year's tax rate. Certain items are given discrete period treatment and, as a result, the tax effects of such items are reported in full in the relevant interim period. The Company's tax rate was 32.7% and 35.0% for the three and nine months ended September 30, 2010 compared to 35.8% and 30.0% for the three and nine months ended September 30, 2009. The Company's tax rate for the three months ended September 30, 2010 was different from the statutory federal income tax rate of 35% primarily because of the release of approximately \$2.3 million of valuation allowances against certain international deferred tax assets, which resulted from the acquisition of dsicmm. During the nine months ended September 30, 2009, DST recorded a \$41.7 million gain on the purchase of the remaining 50% equity interest in Argus with no related income tax expense, reversed approximately \$0.9 million of deferred tax liabilities related to the elimination of deferred tax liabilities previously established for equity in earnings of Argus, and recorded an income tax benefit of approximately \$5.7 million resulting from a reduction in income tax related liabilities principally associated with the completion of an IRS examination in February 2009 for the tax years ended December 31, 2002 through 2005.

The full year 2010 tax rate can be affected as a result of variances among the estimates and amounts of full year sources of taxable income (e.g., domestic consolidated, joint venture and/or international), the realization of tax credits (e.g., historic rehabilitation, research and experimentation, foreign tax and state incentive), adjustments which may arise from the resolution of tax matters under review and the Company's assessment of its liability for uncertain tax positions.

Table of Contents**8. DST Systems, Inc. Stockholders Equity***Earnings per share*

The computation of basic and diluted earnings per share is as follows (in millions, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net income attributable to DST Systems, Inc.	\$ 54.3	\$ 60.9	\$ 225.2	\$ 182.8
Average common shares outstanding	46.6	49.7	47.2	49.7
Incremental shares from restricted stock units and assumed conversions of stock options and debentures	0.3	0.5	0.3	0.3
Average diluted shares outstanding	46.9	50.2	47.5	50.0
Basic earnings per share	\$ 1.17	\$ 1.22	\$ 4.77	\$ 3.68
Diluted earnings per share	\$ 1.16	\$ 1.21	\$ 4.74	\$ 3.65

The Company had approximately 46.2 million and 49.7 million shares outstanding at September 30, 2010 and 2009, respectively. Shares from options to purchase common stock, excluded from the diluted earnings per share calculation because they were anti-dilutive, totaled 3.8 million and 4.0 million for the three and nine months ended September 30, 2010 compared to 2.7 million and 3.3 million for the three and nine months ended September 30, 2009. The Company's convertible senior debentures would have a potentially dilutive effect on the Company's stock if converted in the future. At September 30, 2010, outstanding Series C debentures were convertible into 2.9 million shares of common stock, subject to adjustment. The Company intends to settle any conversions with cash for the principal amount of the bonds and accrued and unpaid interest and issue common stock for any conversion value amount over the principal and accrued and unpaid interest amount. Related to the debentures, the calculation of diluted earnings per share includes an incremental amount of shares assumed to be issued for the conversion spread when the Company's average daily stock price exceeds the average accreted bond price per share. There was no additional dilution for the three and nine months ended September 30, 2010 and 2009 because the Company's average share price was less than the average accreted price per share.

Share Based Compensation

The Company has a share based compensation plan covering its employees. During the nine months ended September 30, 2010, the Company issued approximately 0.2 million common stock options, 0.4 million restricted stock units (RSU's) and exchanged 0.1 million of previously awarded restricted stock shares for the same amount of RSU's. The 0.4 million RSU grants contain performance features and are expected to vest over a three to five year period. Approximately 0.7 million previously issued restricted stock shares vested in January 2010 and in connection with the vesting of those shares, the Company retained approximately 0.3 million vested shares in settlement of employee

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tax-withholding obligations. At September 30, 2010, the Company had outstanding 0.5 million unvested RSU s, 0.2 million unvested restricted shares and 5.7 million stock options (of which 1.3 million are not yet exercisable).

Grants of RSU s are valued at the date of grant based on the value of DST s common stock. The grant date fair value of the 0.4 million RSU s granted during the nine months ended September 30, 2010 was approximately \$16.5 million. Certain of these RSU s contain separate service and performance vesting requirements, while other grants contain performance vesting requirements with service required through the date of certification of performance. The grant date fair value of the awards is generally being amortized over three to five year periods assuming full achievement of the required performance features of the awards. The Company will continue to monitor and evaluate its assumptions over the performance period. Unvested RSU s may be forfeited upon

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termination of employment with the Company depending on the circumstances of the termination. Holders of RSU s are able to participate in cash dividends, if any, (paid in the form of additional RSU s, subject to the same vesting terms as the underlying RSU s), but do not have full stockholders rights, including voting rights, prior to vesting.

At September 30, 2010, the Company had \$24.7 million of total unrecognized compensation expense (included in Additional paid-in-capital on the Condensed Consolidated Balance Sheet) related to its share based compensation arrangements, net of estimated forfeitures. The Company estimates that the amortized compensation expense attributable to the stock option, restricted stock and restricted stock unit grants will be approximately \$5.3 million for the remainder of 2010, \$12.5 million for 2011, \$6.2 million for 2012 and \$0.7 million for 2013, based on awards currently outstanding.

Other comprehensive income (loss)

Components of other comprehensive income (loss) consist of the following (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net income	\$ 54.2	\$ 60.9	\$ 225.1	\$ 182.8
Other comprehensive income (loss):				
Unrealized gains (losses) on investments:				
Unrealized holding gains (losses) arising during the period	63.0	153.9	(72.2)	284.7
Proportional share of unconsolidated affiliate interest rate swap	0.3	0.5	2.7	1.3
Unrealized gain (loss) on interest rate swaps	(1.3)	(2.1)	(4.5)	(1.7)
Less reclassification adjustments for net (gains) losses included in net income	(0.9)	(22.4)	(41.1)	1.3
Foreign currency translation adjustments	23.8	12.1	0.1	43.6
Deferred income taxes	(29.4)	(55.0)	43.4	(122.7)
Other comprehensive income (loss):	55.5	87.0	(71.6)	206.5
Comprehensive income (loss)	\$ 109.7	\$ 147.9	\$ 153.5	\$ 389.3

One of DST s unconsolidated affiliates had an interest rate swap liability with a fair market value of \$67.5 million and \$35.6 million at September 30, 2010 and December 31, 2009, respectively. DST s 50% proportionate share of this interest rate swap liability was \$33.7 million and \$17.8 million at September 30, 2010 and December 31, 2009, respectively. The Company records in investments and accumulated other comprehensive income its proportionate share of this liability in an amount not to exceed the carrying value of its investment in this unconsolidated affiliate. At September 30, 2010 and December 31, 2009, the Company s proportionate share of this liability (in an amount not to exceed the carrying value of its investment in this unconsolidated affiliate) was \$2.3 million and \$5.0 million, respectively.

Stock repurchases

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On May 11, 2010, DST's Board of Directors authorized the repurchase of an additional 1.0 million shares under the existing share repurchase authorization plan, which allows for the repurchase of common stock in open market and private transactions through December 31, 2012. At September 30, 2010, there were approximately 0.5 million shares remaining to be repurchased under the Company's existing share repurchase authorization plan. The Company repurchased 0.5 million shares of DST common stock for \$21.2 million or approximately \$41.17

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per share during the three months ended September 30, 2010. The Company repurchased 2.8 million shares of DST common stock for \$112.3 million or approximately \$40.28 per share during the nine months ended September 30, 2010.

Dividends declared

On March 4, 2010, DST declared its first cash dividend since going public in 1995 and paid a \$0.30 per share dividend on April 8, 2010 to shareholders of record as of the close of business on March 17, 2010. The aggregate amount of the cash dividend was \$14.3 million.

On October 6, 2010, DST declared a cash dividend of \$0.30 per share and paid the dividend on November 5, 2010 to shareholders of record as of the close of business on October 21, 2010. The aggregate amount of this cash dividend was approximately \$13.9 million.

9. Commitments and Contingencies

The Company and its subsidiaries are involved in various legal proceedings arising in the normal course of their businesses. While the ultimate outcome of these legal proceedings cannot be predicted with certainty, it is the opinion of management, after consultation with legal counsel, that the final outcome in such proceedings, in the aggregate, would not have a material adverse effect on the consolidated financial condition, results of operations and cash flows of the Company.

The Company has letters of credit of \$8.0 million and \$8.3 million outstanding at September 30, 2010 and December 31, 2009, respectively. Letters of credit are secured by the Company's debt facility.

The Company has entered into agreements with certain officers whereby upon defined circumstances constituting a change in control of the Company, certain benefit entitlements are automatically funded and such officers are entitled to specific cash payments upon termination of employment.

The Company has established trusts to provide for the funding of corporate commitments and entitlements of Company officers, directors, employees and others in the event of a change in control of the Company. Assets held in such trusts at September 30, 2010 and December 31, 2009 were not significant.

The Company has entered into an agreement to guarantee 50% of the obligations of a 50% owned joint venture as a tenant under a real estate lease for an office building. The initial term of the lease is 10 years and 7 months, commencing March 1, 2007 and expiring September 30, 2017, with two five-year options to extend. The base rent for the initial term is \$4.8 million per year, plus all operating expenses for the building.

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The Company entered into an agreement to guarantee \$2.0 million plus any enforcement costs related to a \$32.0 million mortgage loan to a 33% owned real estate joint venture. The \$32.0 million loan matures on June 30, 2013. At September 30, 2010 and December 31, 2009, total borrowings on the loan were \$30.6 million and \$31.1 million, respectively, and the Company's guarantee totaled \$1.0 million for both September 30, 2010 and December 31, 2009.

In April 2010, the Company entered into an agreement to guarantee 29% of the outstanding principal amount related to a mortgage loan to a 50% owned real estate joint venture. The loan matures on April 2015. At September 30, 2010 total borrowings on the loan were \$13.5 million and the Company's guarantee was approximately \$3.9 million.

The Company's 50% owned joint ventures are generally governed by shareholder or partnership agreements. The agreements generally entitle the Company to elect one-half of the directors to the board in the case of corporations and to have 50% voting/managing interest in the case of partnerships. The agreements generally provide that the Company or the other party has the option to establish a price payable in cash, or a promise to pay cash, for all of the other's ownership in the joint venture and to submit an offer, in writing, to the other party to sell to the other party all of its ownership interests in the joint venture or to purchase all ownership interests owned by the other party at such offering price. The party receiving the offer generally has a specified period of time to either accept the offer to purchase, or to elect to purchase the offering party's interest at the offering price. The Company

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cannot estimate the potential aggregate offering price that it could be required to receive or elect to pay in the event this option becomes operable; however, the amount could be material.

Guarantees

In addition to the guarantees entered into as mentioned above, the Company has also guaranteed certain obligations of certain joint ventures under service agreements entered into by the joint ventures and their customers. The amount of such obligations is not stated in the agreements. Depending on the negotiated terms of the guaranty and/or the underlying service agreement, the Company's liability under the guaranty may be subject to time and materiality limitations, monetary caps and other conditions and defenses.

In certain instances in which the Company licenses proprietary systems to customers, the Company gives certain warranties and infringement indemnities to the licensee, the terms of which vary depending on the negotiated terms of each respective license agreement, but which generally warrant that such systems will perform in accordance with their specifications. The amount of such obligations is not stated in the license agreements. The Company's liability for breach of such warranties may be subject to time and materiality limitations, monetary caps and other conditions and defenses.

From time to time, the Company enters into agreements with unaffiliated parties containing indemnification provisions, the terms of which vary depending on the negotiated terms of each respective agreement. The amount of such obligations is not stated in the agreements. The Company's liability under such indemnification provisions may be subject to time and materiality limitations, monetary caps and other conditions and defenses. Such indemnity obligations include the following:

The Company has entered into purchase and service agreements with its vendors, and consulting agreements with providers of consulting services to the Company, pursuant to which the Company has agreed to indemnify certain of such vendors and consultants, respectively, against third party claims arising from the Company's use of the vendor's product or the services of the vendor or consultant.

In connection with the acquisition or disposition of subsidiaries, operating units and business assets by the Company, the Company has entered into agreements containing indemnification provisions, the terms of which vary depending on the negotiated terms of each respective agreement, but which are generally described as follows: (i) in connection with acquisitions made by the Company, the Company has agreed to indemnify the seller against third party claims made against the seller relating to the subject subsidiary, operating unit or asset and arising after the closing of the transaction, and (ii) in connection with dispositions made by the Company, the Company has agreed to indemnify the buyer against damages incurred by the buyer due to the buyer's reliance on representations and warranties relating to the subject subsidiary, operating unit or business assets in the disposition agreement if such representations or warranties were untrue when made, or due to any breach of the representations, warranties, agreements or covenants contained in the agreement.

The Company has entered into agreements with certain third parties, including banks and escrow agents that provide software escrow, fiduciary and other services to the Company or to its benefit plans or customers. Under such agreements, the Company has agreed to indemnify such service providers for third party claims relating to the carrying out of their respective duties under such agreements.

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The Company has entered into agreements with lenders providing financing to the Company pursuant to which the Company agrees to indemnify such lenders for third party claims arising from or relating to such financings. In connection with real estate mortgage financing, the Company has entered into environmental indemnity agreements in which the Company has agreed to indemnify the lenders for any damage sustained by the lenders relating to any environmental contamination on the subject properties.

In connection with the acquisition or disposition of real estate by the Company, the Company has entered into real estate contracts containing indemnification provisions, the terms of which vary depending on the negotiated terms of each respective contract, but which are generally described as follows: (i) in connection with acquisitions by the Company, the Company has agreed to indemnify the seller against third party claims made against the seller

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arising from the Company's on-site inspections, tests and investigations of the subject property made by the Company as part of its due diligence and against third party claims relating to the operations on the subject property after the closing of the transaction, and (ii) in connection with dispositions by the Company, the Company has agreed to indemnify the buyer for damages incurred by the buyer due to the buyer's reliance on representations and warranties relating to the subject property made by the Company in the real estate contract if such representations or warranties were untrue when made and against third party claims relating to operations on the subject property prior to the closing of the transaction.

In connection with the leasing of real estate by the Company, as landlord and as tenant, the Company has entered into occupancy leases containing indemnification provisions, the terms of which vary depending on the negotiated terms of each respective lease, but which are generally described as follows: (i) in connection with leases in which the Company is the tenant, the Company has agreed to indemnify the landlord against third party claims relating to the Company's occupancy of the subject property, including claims arising from loss of life, bodily injury and/or damage to property thereon, and (ii) in connection with leases in which the Company is the landlord, the Company has agreed to indemnify the tenant against third party claims to the extent occasioned wholly or in part by any negligent act or omission of the Company or arising from loss of life, bodily injury and/or damage to property in or upon any of the common areas or other areas under the Company's control.

At September 30, 2010 and December 31, 2009, the Company had not accrued any liability on the aforementioned guarantees or indemnifications as they relate to future performance criteria or indirect guarantees of indebtedness of others in accordance with accounting and reporting guidance on guarantees, including indirect guarantees of indebtedness of others.

10. Restructuring Charge

On January 29, 2010, DST began implementing a plan to reduce its workforce by approximately 7% in 2010. This plan was necessitated by the extended economic downturn which has negatively impacted the financial services industry. The reduction in workforce is part of the Company's ongoing cost management initiatives which have included a general freeze on hiring and management salaries, and other controls over operating expenses. As a result of this workforce reduction, the Company anticipates a \$19.5 million pre-tax charge in 2010 for the payment of related termination benefits. The Company incurred \$2.8 million and \$17.4 million of termination benefit expense associated with this plan during the three and nine months ended September 30, 2010 and expects approximately \$2.1 million of related expenses for the remainder of 2010. These termination benefit expenses have been included in Costs and expenses in the Condensed Consolidated Statement of Income. The Company is approximately 90% complete with the workforce reduction plan as of September 30, 2010.

The following table (in millions) presents termination benefit expenses at September 30, 2010 and summarizes the remainder of 2010 restructuring activities described above.

		Plan Estimate, as Revised	Costs Paid or Settled Nine Months Ended September 30, 2010	Estimated Remaining Settlement Three Months Ended December 31, 2010
Financial Services	\$	13.5	\$ (12.1)	\$ 1.4
Output Solutions		6.0	(5.3)	0.7
	\$	19.5	\$ (17.4)	\$ 2.1

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11. Authoritative Accounting Guidance

Variable Interest Entities

On January 1, 2010, the Company adopted new authoritative accounting guidance related to variable interest entities. Among other items, this accounting guidance responds to concerns about the application of certain key provisions of the current accounting guidance for variable interest entities, including those regarding the transparency of the involvement with variable interest entities. The adoption of this new accounting guidance did not have a significant impact on the consolidated financial statements.

Multiple-Element Revenue Arrangements

In October 2009, the FASB issued new authoritative accounting guidance related to multiple element revenue arrangements. This update provides guidance on whether multiple elements (deliverables) exist, how the deliverables should be separated and how the consideration should be allocated. The new guidance established a hierarchy for determining the selling price of a deliverable. For DST, the new authoritative guidance is effective prospectively for revenue arrangements entered into or materially modified after January 1, 2011. Early adoption is permitted. The Company has not determined the impact this new authoritative accounting guidance may have on the consolidated financial statements.

Certain Revenue Arrangements That Include Software Elements

In October 2009, the FASB issued new authoritative accounting guidance related to certain revenue arrangements that include software elements. This new guidance changes the accounting model for revenue arrangements that include both tangible products and software elements and also provides guidance on how consideration should be allocated in an arrangement that includes both tangible products and software. For DST, the new authoritative guidance is effective prospectively for revenue arrangements entered into or materially modified after January 1, 2011. Early adoption is permitted. The Company has not determined the impact this guidance may have on the consolidated financial statements.

Earnings per Share Proposed Accounting Standard

In August 2008, the FASB issued a revised exposure draft, that would amend current earnings per share accounting guidance to clarify guidance for mandatorily convertible instruments, the treasury stock method, contingently issuable shares, and contracts that may be settled in cash or shares. The final authoritative accounting guidance has yet to be issued. In April 2009, the FASB decided to pause the earnings per share project.

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The proposed guidance, which is designed for convergence with international accounting standards, would require the use of the if-converted method from the date of issuance of the convertible debentures. The proposed guidance would remove the ability of a company to support the presumption that the convertible securities will be satisfied in cash and not converted into shares of common stock. Accordingly, the Company's stated intention to settle conversions of its convertible debentures with cash for the principal and accrued and unpaid interest and issue common stock for any conversion value amount over the principal and accrued and unpaid interest amounts would no longer be accepted under the proposed guidance. Retrospective application would be required for all changes, except that retrospective application would be prohibited for contracts that were either settled in cash prior to adoption or modified prior to adoption to require cash settlement. For DST, adoption of this accounting guidance, as proposed, will require retroactive restatement of the Company's diluted earnings per share calculations subsequent to the issuance of the convertible debentures. In calculating diluted earnings per share using the if-converted method included in the exposure draft, the Company would need to increase net income for the interest expense associated with the convertible debentures, net of tax, and increase the incremental shares assumed to be issued upon conversion by approximately 2.9 million shares (less shares already included in diluted earnings per share, if any), the amount of shares that would be issued if all \$143.6 million of the senior convertible debentures at September 30, 2010 would be converted to equity. The revised exposure draft also contains other EPS computational changes (e.g., treasury stock method considerations) that may have an effect on

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the Company's diluted earnings per share calculation. DST is continuing to monitor the FASB's progress towards finalizing this proposed accounting guidance.

The proposed change in accounting principle would affect the calculation of diluted earnings per share during the period the debentures are outstanding, but would not affect DST's ability to ultimately settle the convertible debentures in cash, shares or any combination thereof. The estimated impact of this new accounting guidance reflects the Company's current estimates based upon the exposure draft in its current form. There may be material differences between these estimates and the actual impact of the guidance when issued as final.

12. Segment Information

The Company's operating business units offer sophisticated information processing and software services and products. The Company has elected to organize and report on these business units as two operating segments (Financial Services and Output Solutions). In addition, investments in the Company's real estate subsidiaries and affiliates, equity securities, private equity investments and certain financial interests have been aggregated into an Investments and Other Segment.

Information concerning total assets by reporting segment is as follows (in millions):

	September 30, 2010	December 31, 2009
Financial Services	\$ 1,506.3	\$ 1,477.8
Output Solutions	452.0	253.4
Investments and Other	1,159.3	1,267.0
Elimination Adjustments	(85.4)	(85.4)
	\$ 3,032.2	\$ 2,912.8

The Company evaluates the performance of its Segments based on income before income taxes, interest expense and non-controlling interest. Intersegment revenues are reflected at rates prescribed by the Company and may not be reflective of market rates.

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Summarized financial information concerning the Company's Segments is shown in the following tables (in millions):

	Three Months Ended September 30, 2010				
	Financial Services	Output Solutions	Investments / Other	Eliminations Adjustments	Consolidated Total
Operating revenues	\$ 287.3	\$ 128.7	\$ 3.0	\$	\$ 419.0
Intersegment operating revenues	3.1	2.0	11.6	(16.7)	
Out-of-pocket reimbursements	11.5	138.0	0.1	(1.4)	148.2
Total revenues	301.9	268.7	14.7	(18.1)	567.2
Costs and expenses	209.6	255.5	9.7	(15.5)	459.3
Depreciation and amortization	19.5	12.2	2.5	(0.7)	33.5
Income (loss) from operations	72.8	1.0	2.5	(1.9)	74.4
Other income (loss), net	0.7		8.7		9.4
Equity in earnings of unconsolidated affiliates	8.8		0.1		8.9
Earnings (loss) before interest, income taxes and non-controlling interest	\$ 82.3	\$ 1.0	\$ 11.3	\$ (1.9)	\$ 92.7

	Three Months Ended September 30, 2009				
	Financial Services	Output Solutions	Investments / Other	Eliminations Adjustments	Consolidated Total
Operating revenues	\$ 273.9	\$ 118.7	\$ 3.0	\$	\$ 395.6
Intersegment operating revenues	2.4	1.6	12.1	(16.1)	
Out-of-pocket reimbursements	11.6	145.5	0.1	(1.1)	156.1
Total revenues	287.9	265.8	15.2	(17.2)	551.7
Costs and expenses	211.4	248.1	9.7	(14.6)	454.6
Depreciation and amortization	20.9	10.7	3.6	(0.7)	34.5
Income (loss) from operations	55.6	7.0	1.9	(1.9)	62.6
Other income, net		0.2	32.9	0.1	33.2
Equity in earnings of unconsolidated affiliates	7.8				7.8
Earnings (loss) before interest, income taxes and non-controlling interest	\$ 63.4	\$ 7.2	\$ 34.8	\$ (1.8)	\$ 103.6

Earnings before interest and income taxes in the segment reporting information above less interest expense of \$12.1 million and \$8.8 million for the three months ended September 30, 2010 and 2009, respectively, is equal to the Company's income before income taxes and non-controlling interest on a consolidated basis for the corresponding periods.

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	Nine Months Ended September 30, 2010				
	Financial Services	Output Solutions	Investments / Other	Eliminations Adjustments	Consolidated Total
Operating revenues	\$ 855.7	\$ 428.9	\$ 9.4	\$	\$ 1,294.0
Intersegment operating revenues	8.3	5.9	34.6	(48.8)	
Out-of-pocket reimbursements	35.2	422.7	0.3	(4.4)	453.8
Total revenues	899.2	857.5	44.3	(53.2)	1,747.8
Costs and expenses	637.9	742.7	28.2	(45.4)	1,363.4
Depreciation and amortization	58.7	35.2	7.5	(2.0)	99.4
Income (loss) from operations	202.6	79.6	8.6	(5.8)	285.0
Other income (loss), net	8.1	0.1	59.6		67.8
Equity in earnings of unconsolidated affiliates	26.5		0.5		27.0
Earnings (loss) before interest, income taxes and non-controlling interest	\$ 237.2	\$ 79.7	\$ 68.7	\$ (5.8)	\$ 379.8

	Nine Months Ended September 30, 2009				
	Financial Services	Output Solutions	Investments / Other	Eliminations Adjustments	Consolidated Total
Operating revenues	\$ 825.0	\$ 361.6	\$ 9.1	\$	\$ 1,195.7
Intersegment operating revenues	6.7	3.2	35.9	(45.8)	
Out-of-pocket reimbursements	41.6	431.5	0.4	(2.6)	470.9
Total revenues	873.3	796.3	45.4	(48.4)	1,666.6
Costs and expenses	632.3	746.6	29.0	(40.6)	1,367.3
Depreciation and amortization	57.5	29.6	8.7	(2.0)	93.8
Income (loss) from operations	183.5	20.1	7.7	(5.8)	205.5
Other income, net	41.6	0.4	18.6		60.6
Equity in earnings of unconsolidated affiliates	24.3		(0.3)		24.0
Earnings (loss) before interest, income taxes and non-controlling interest	\$ 249.4	\$ 20.5	\$ 26.0	\$ (5.8)	\$ 290.1

Earnings before interest and income taxes in the segment reporting information above less interest expense of \$33.7 million and \$28.9 million for the nine months ended September 30, 2010 and 2009, respectively, is equal to the Company's income before income taxes and non-controlling interest on a consolidated basis for the corresponding periods.

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

The discussions set forth in this Quarterly Report on Form 10-Q contain statements concerning potential future events. Such forward-looking statements are based upon assumptions by the Company's management as of the date of this Quarterly Report, including assumptions about risks and uncertainties faced by the Company. In addition, management may make forward-looking statements orally or in other writings, including, but not limited to, in press releases, in the annual report to shareholders and in the Company's other filings with the Securities and Exchange Commission (SEC). Readers can identify these forward-looking statements by the use of such verbs as expects, anticipates, believes or similar verbs or conjugations of such verbs. If any of management's assumptions prove incorrect or should unanticipated circumstances arise, the Company's actual results could materially differ from those anticipated by such forward-looking statements. The differences could be caused by a number of factors or combination of factors including, but not limited to, those factors referred to below in Part II, Item 1A, Risk Factors. Readers are strongly encouraged to consider the factors referred to in such section and any amendments or modifications thereof when evaluating any forward-looking statements concerning the Company. The Company's reports filed with or furnished to the SEC on Form 8-K, Form 10-K, Form 10-Q and other forms and any amendments to those reports, may be obtained by contacting the SEC's Public Reference Branch at 1-800-SEC-0330 or by accessing the forms electronically, free of charge, through the SEC's Internet website at <http://www.sec.gov> or through the Company's Internet website, as soon as reasonably practicable after filing with the SEC, at <http://www.dstsystems.com>. The Company undertakes no obligation to update any forward-looking statements in this Quarterly Report to reflect future events or developments.

The information contained in this Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the Condensed Consolidated Financial Statements and Notes thereto included in this Form 10-Q and the audited Consolidated Financial Statements and Notes thereto in the Company's Annual Report on Form 10-K for the year ended December 31, 2009.

INTRODUCTION

The business units of DST Systems, Inc. (DST or the Company) offer sophisticated information processing and software services and products. These business units are reported as two operating segments, Financial Services and Output Solutions. In addition, investments in the Company's real estate subsidiaries and affiliates, equity securities, private equity funds and certain financial interests have been aggregated into the Investments and Other Segment.

A summary of each of the Company's Segments follows:

Financial Services

The Company's Financial Services Segment provides sophisticated information processing and computer software services and products using proprietary software systems primarily to mutual funds, investment managers, insurance companies, healthcare providers, banks, brokers, financial planners, healthcare payers, real estate partnerships, third party administrators and medical practice groups. The Company's proprietary software systems include mutual fund shareowner, subaccount and unit trust recordkeeping systems for U.S. and international mutual fund companies; a defined contribution participant recordkeeping system for the U.S. retirement plan market; platforms for distribution support solutions and services offered to financial advisors and broker/dealers; investment management systems offered to U.S. and international

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investment managers and fund accountants; a business process management and customer contact system offered to mutual funds, insurance companies, brokerage firms, banks, healthcare payers, healthcare providers, cable television operators and mortgage servicing organizations; healthcare claims administration processing systems and services offered to providers of healthcare plans, third party administrators and medical practice groups; pharmacy claims processing systems offered to healthcare plans, insurance companies, third party administrators and pharmacy benefit managers; and an electronic file system offered to mutual fund companies, insurance companies and professional service (legal, accounting and others) firms.

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The Financial Services Segment distributes its services and products on a direct basis and through subsidiaries and joint venture affiliates in the U.S., United Kingdom (U.K.), Canada, Europe, Australia, South Africa, Asia-Pacific and the Middle East and, to a lesser degree, distributes such services and products through various strategic alliances.

Output Solutions

The Company's Output Solutions Segment provides single source, integrated print and electronic statement and billing output solutions, including customized statement and bill production, marketing and personalization services, postal optimization, and electronic presentment, payment and distribution solutions. These capabilities enable the Output Solutions Segment to provide services to industries that place a premium on customer communications that require high quality, accurate and timely statement and billing output processing.

On July 30, 2010, DST, through its wholly-owned U.K. subsidiary, Innovative Output Solutions Limited (IOS), acquired dsicmm Group Limited (dsicmm), a provider of print/mail services in the U.K., for cash and the issuance of IOS stock. After completion of the transaction, DST will own approximately 70.5% of IOS and the remaining 29.5% will be owned by a group of the former stockholders of dsicmm. DST has consolidated the financial results of the combined IOS business from the closing date and has reflected the 29.5% owned by the former stockholders of dsicmm as a non-controlling interest.

The Output Solutions Segment conducts its operations from four operating facilities located throughout North America and six operating facilities located throughout the U.K. DST Output is among the largest users of continuous, high-speed, full-color inkjet printing systems and among the largest First-class mailers in the U.S. IOS is among the largest direct communications manufacturers in the U.K.

The Output Solutions Segment's research and development efforts have resulted in two mail and postal processing initiatives, Smart Commingling and Intelligent Mail barcode, in compliance with United States Postal Services requirements. In addition, the Digital Press Technology (DPT) high-speed color printing and inserting platform enables the Output Solutions Segment to produce high-speed transactional printing combined with dynamic color printing. DST Output believes DPT is a technologically-differentiated service offering that enables them to provide better and more efficient products and services to clients.

The Output Solutions Segment distributes its product directly to customers and through relationships in which its services are combined with or offered concurrently through providers of data processing services. The Output Solutions Segment's products are also distributed or bundled with product offerings to customers of the Financial Services Segment.

Investments and Other

The Investments and Other Segment is comprised of the Company's real estate subsidiaries and affiliates, investments in equity securities, private equity funds and other financial interests. The assets held by the Investments and Other Segment are primarily passive in nature. The Company owns and operates real estate mostly in the U.S. and U.K., which is held primarily for lease to the Company's other business segments. The Company is a partner in certain real estate joint ventures that lease office space to the Company, certain of its unconsolidated affiliates and

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unrelated third parties. The Company is a 50% partner in a limited purpose real estate joint venture formed to develop and lease approximately 1.1 million square feet of office space to the U.S. government. The Investments and Other Segment holds investments in available-for-sale equity securities with a market value of approximately \$731.5 million at September 30, 2010, including approximately 10.6 million shares of State Street Corporation (State Street), 17.5 million shares of Computershare Ltd. (Computershare) and 1.9 million shares of Euronet Worldwide, Inc., with a market value of \$398.5 million, \$165.0 million and \$33.9 million, respectively, based on closing exchange values at September 30, 2010.

Table of Contents**RESULTS OF OPERATIONS**

The following table summarizes the Company's operating results (in millions, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenues				
Operating revenues				
Financial Services	\$ 290.4	\$ 276.3	\$ 864.0	\$ 831.7
Output Solutions	130.7	120.3	434.8	364.8
Investments and Other	14.6	15.1	44.0	45.0
Elimination Adjustments	(16.7)	(16.1)	(48.8)	(45.8)
	419.0	395.6	1,294.0	1,195.7
% change from prior year period	5.9%		8.2%	
Out-of-pocket reimbursements				
Financial Services	11.5	11.6	35.2	41.6
Output Solutions	138.0	145.5	422.7	431.5
Investments and Other	0.1	0.1	0.3	0.4
Elimination Adjustments	(1.4)	(1.1)	(4.4)	(2.6)
	148.2	156.1	453.8	470.9
% change from prior year period	(5.1)%		(3.6)%	
Total revenues	\$ 567.2	\$ 551.7	\$ 1,747.8	\$ 1,666.6
% change from prior year period	2.8%		4.9%	
Income from operations				
Financial Services	\$ 72.8	\$ 55.6	\$ 202.6	\$ 183.5
Output Solutions	1.0	7.0	79.6	20.1
Investments and Other	2.5	1.9	8.6	7.7
Elimination Adjustments	(1.9)	(1.9)	(5.8)	(5.8)
	74.4	62.6	285.0	205.5
Interest expense	(12.1)	(8.8)	(33.7)	(28.9)
Other income, net	9.4	33.2	67.8	60.6
Equity in earnings of unconsolidated affiliates	8.9	7.8	27.0	24.0
Income before income taxes and non-controlling interest	80.6	94.8	346.1	261.2
Income taxes	26.4	33.9	121.0	78.4
Net income	54.2	60.9	225.1	182.8
Noncontrolling interest	0.1		0.1	
Net income attributable to DST Systems, Inc.	\$ 54.3	\$ 60.9	\$ 225.2	\$ 182.8
Basic earnings per share	\$ 1.17	\$ 1.22	\$ 4.77	\$ 3.68
Diluted earnings per share	\$ 1.16	\$ 1.21	\$ 4.74	\$ 3.65
Non-GAAP diluted earnings per share	\$ 1.03	\$ 0.94	\$ 3.36	\$ 2.67
Cash dividends per share of common stock	\$	\$	\$ 0.30	\$

Table of Contents**Consolidated revenues**

Consolidated total revenues (including out-of-pocket (OOP) reimbursements) for the three and nine months ended September 30, 2010 were \$567.2 million and \$1,747.8 million, an increase of \$15.5 million or 2.8% and \$81.2 million or 4.9% compared to the three and nine months ended September 30, 2009. Consolidated operating revenues for the three and nine months ended September 30, 2010 increased \$23.4 million or 5.9% and \$98.3 million or 8.2% compared to the same periods in 2009. The increases in consolidated operating revenues are attributable to increases of \$14.1 million and \$32.3 million in the Financial Services Segment for the three and nine months ended September 30, 2010 and increases of \$10.4 million and \$70.0 million in the Output Solutions Segment for the three and nine months ended September 30, 2010, both as compared to the same periods in 2009. In the third quarter 2010, the Company received a contract termination payment for a subaccounting client of \$10.4 million (\$9.1 million in the Financial Services Segment and \$1.3 million in the Output Solutions Segment). In addition, the Company acquired dsicmm Group Limited (dsicmm), a provider of print/mail services in the U.K., on July 30, 2010, which contributed \$22.0 million of operating revenues to the Output Solutions Segment during third quarter 2010. Excluding dsicmm operating revenues and the contract termination payment received in third quarter 2010, consolidated operating revenue decreased \$9.0 million or 2.3%, compared to the same period in 2009. On this basis, Financial Services operating revenues increased \$5.0 million or 1.8% during third quarter 2010 as compared to the same period in 2009, and Output Solutions operating revenues decreased \$12.9 million or 10.7%, principally from the termination of an Output Solutions client processing agreement on April 30, 2010. As previously announced, an Output Solutions telecommunications client, representing approximately 6.6% of 2009 annual Output Solutions Segment operating revenues, terminated its contract and internalized its bill production processing, which resulted in a contract termination payment to the Company of approximately \$63.0 million.

As mentioned above, consolidated operating revenues increased \$98.3 million during the nine months ended September 30, 2010, mostly comprised of \$32.3 million in Financial Services and \$70.0 million in Output Solutions. Excluding contract termination payments of \$9.1 million in Financial Services and \$64.3 million in Output Solutions mentioned above, Output Solutions operating revenues resulting from the acquisition of dsicmm of \$22.0 million and net incremental Financial Services operating revenues resulting from the acquisition and consolidation of Argus Health Systems (Argus) on March 31, 2009 of \$26.0 million, consolidated operating revenues for the nine months ended September 30, 2010 decreased \$23.1 million or 1.9%, compared to the same period in 2009. On this basis, Financial Services Segment operating revenues decreased \$2.8 million or 0.3% and Output Solutions decreased \$16.3 million or 4.5% during the nine months ended September 30, 2010 as compared to 2009. On this basis, the decrease in Financial Services operating revenues is attributable to lower DST Health Solutions revenues, partially offset by higher Global Solutions and Argus revenues. This operating revenue decrease was partially offset by changes in foreign currency exchange rates which increased operating revenues by approximately \$9.2 million. On this basis, the Output Solutions decrease is mostly due to the loss of revenues from a terminated telecommunications client, lower volumes from existing clients and lower revenue per unit (images produced and items mailed) processed.

Consolidated OOP reimbursements during the three and nine months ended September 30, 2010 decreased \$7.9 million or 5.1% and \$17.1 million or 3.6% compared to the same periods in 2009. OOP reimbursements for Output Solutions decreased \$7.5 million or 5.2% during the three months ended September 30, 2010 and \$8.8 million or 2.0% during the nine months ended September 30, 2010, both compared to the same periods in 2009, primarily due to a contract termination mentioned above and lower processing volumes.

Income from operations

Consolidated income from operations for the three and nine months ended September 30, 2010 increased \$11.8 million or 18.8% and \$79.5 million or 38.7% compared to the three and nine months ended September 30, 2009. Absent the subaccounting contract termination payment received in third quarter 2010 (\$9.1 million in Financial Services and \$1.3 million in Output Solutions), expenses associated with the client contract termination of \$1.6 million in Financial Services and termination benefit costs of \$2.8 million (\$0.7 million in Financial Services and \$2.1 million in Output Solutions) related to a reduction in workforce, income from operations increased \$5.8 million or 9.3% during the three

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months ended September 30, 2010 compared to the same period in 2009. On this

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basis, Financial Services income from operations increased \$10.4 million or 18.7% to \$66.0 million during third quarter 2010 quarter from higher revenues and lower operating expenses. Output Solutions income from operations, before considering a dsicmm loss from operations of \$2.9 million, decreased \$2.3 million or 32.9% to \$4.7 million during the quarter from reduced operating revenues.

Absent the contract termination payments and related expense during the three months ended September 30, 2010 mentioned above, the \$63.0 million Output Solutions contract termination payment received in April 2010, expenses associated with the Output Solutions client contract termination (including asset impairment charges of \$3.1 million and termination benefit costs of \$1.5 million) and termination benefit costs of \$17.4 million related to a previously announced reduction in workforce (\$12.1 million in Financial Services and \$5.3 million in Output Solutions), income from operations increased \$29.7 million or 14.5% during the nine months ended September 30, 2010 as compared to the same period in 2009. On this basis, Financial Services income from operations increased \$23.7 million or 12.9% to \$207.2 million during the nine months ended September 30, 2010 from higher revenues and lower operating expenses. Output Solutions income from operations increased \$5.1 million or 25.4% to \$25.2 million during the nine months ended September 30, 2010 from lower operating expenses, partially offset by a \$2.9 million operating loss from dsicmm in third quarter 2010.

Restructuring Charge - Reduction in Workforce

In first quarter 2010, DST began implementing a plan to reduce its workforce by approximately 7% in 2010. This plan was necessitated by the extended economic downturn which has negatively impacted the financial services industry. The reduction in workforce is part of the Company's ongoing cost management initiatives which have included a general freeze on hiring and management salaries, and other controls over operating expenses. As a result of this workforce reduction, the Company anticipates a \$19.5 million pre-tax charge in 2010 for the payment of related termination benefits. The Company incurred \$2.8 million and \$17.4 million of termination benefit expense during the three and nine months ended September 30, 2010 and expects approximately \$2.1 million of related expenses for the remainder of 2010. These termination benefit expenses have been included in Costs and expenses in the Condensed Consolidated Statement of Income. The Company is approximately 90% complete with the workforce reduction plan as of September 30, 2010.

The following table (in millions) presents termination benefit expenses at September 30, 2010 and summarizes the remainder of 2010 restructuring activities described above.

	Plan Estimate, as Revised	Costs Paid or Settled Nine Months Ended September 30, 2010	Estimated Remaining Settlement Three Months Ended December 31, 2010
Financial Services	\$ 13.5	\$ (12.1)	\$ 1.4
Output Solutions	6.0	(5.3)	0.7
	\$ 19.5	\$ (17.4)	\$ 2.1

Interest expense

Interest expense for the three and nine months ended September 30, 2010 was \$12.1 million and \$33.7 million, an increase of \$3.3 million or 37.5% and \$4.8 million or 16.6% compared to the same periods in 2009. Interest expense increased for the three and nine months ended

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September 30, 2010 primarily from higher weighted average interest rates on the Company's syndicated revolving credit facility which was renewed on April 16, 2010 and the privately placed senior notes issued in August 2010, and from recording accounts receivable securitization program costs as interest expense beginning January 1, 2010, partially offset by lower average debt balances during the nine months ended September 30, 2010.

As previously announced, on August 9, 2010, the Company issued \$370.0 million of privately placed senior notes. The senior notes are comprised of \$40.0 million of 4.19% Series A Senior Notes due August 9, 2015,

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\$105.0 million of 4.86% Series B Senior Notes due August 9, 2017, \$65.0 million of 5.06% Series C Senior Notes due August 9, 2018 and \$160.0 million of 5.42% Series D Senior Notes due August 9, 2020. On September 9, 2010 the Company redeemed \$84.1 million of the Series A debentures and \$168.5 million of the Series B debentures, which fully retired these series of debentures. In addition to the Series A and B redemption, the Company repurchased \$35.0 million of aggregate principal of the Series C convertible debentures for \$36.1 million, resulting in a pretax loss of approximately \$1.1 million (included in other income) in third quarter 2010. At September 30, 2010, the Company had approximately \$143.6 million of Series C convertible debentures outstanding. Beginning August 15, 2013, the Company may redeem for cash all or part of the Series C debentures.

Other income, net

The components of other income, net are as follows (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Gain on equity interest in Argus Health Systems	\$	\$	\$	\$ 41.7
Other than temporary impairments / unrealized losses on available-for-sale securities		(0.3)	(0.7)	(26.8)
Net gains (losses) on private equity funds and other investments		1.3	(0.2)	2.6
Net realized gains from sale of available-for-sale securities		1.2	22.5	41.8
Net gain (loss) on extinguishment of senior convertible debentures		(1.1)	0.1	(1.0)
Dividend income		4.0	4.1	17.0
Interest income		1.3	1.5	4.3
Miscellaneous items		3.0	5.2	3.8
Other income, net	\$	9.4	\$ 33.2	\$ 60.6

Other income, net was \$9.4 million and \$67.8 million during the three and nine months ended September 30, 2010 compared to \$33.2 million and \$60.6 million during the three and nine months ended September 30, 2009.

The Company recorded a gain of \$41.7 million during 2009 related to its purchase of the remaining 50% equity interest of Argus for \$57.0 million. In accordance with authoritative accounting guidance on business combinations, the acquisition of the remaining 50% of Argus on March 31, 2009 was treated as a step acquisition. Accordingly, DST remeasured its previously held equity interest in Argus to fair value, in the amount of \$57.0 million, and recorded a gain of \$41.7 million.

The Company records investment impairment charges for available-for-sale securities with gross unrealized holding losses resulting from a decline in value that is other than temporary. The Company recognized \$0.3 million and \$0.7 million of investment impairments for the three and nine months ended September 30, 2010 compared to \$26.8 million for the nine months ended September 30, 2009, which were other than temporary. There were no investment impairments on available-for-sale securities for the three months ended September 30, 2009. The decrease in impairments compared to the same periods in 2009 is from improved financial market conditions. Future adverse changes in market conditions or poor operating results of underlying investments could result in losses or an inability to recover the carrying value of the

investments that may not be reflected in an investment's current carrying value, thereby possibly requiring an impairment charge in the future, which could have a material effect on the Company's financial position.

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Net realized gains from the sale of available-for-sale securities were \$1.2 million and \$41.8 million during the three and nine months ended September 30, 2010, respectively, compared to \$22.5 million and \$25.9 million during the three and nine months ended September 30, 2009, respectively. Included in the \$41.8 million of gains from the sale of available-for-sale securities for the nine months ended September 30, 2010 is a \$28.8 million gain from the sale of approximately 4.8 million shares of Computershare Ltd. Included in the \$25.9 million of gains from the sale of available-for-sale securities for the nine months ended September 30, 2009 is a \$17.6 million gain from the sale of approximately 4.6 million shares of Computershare Ltd.

During the three and nine months ended September 30, 2010, the Company recorded a net loss of \$1.1 million and \$1.0 million, respectively, associated with the repurchase of a portion of the Company's senior convertible debentures at a premium to carrying value. During the three and nine months ended September 30, 2009, the Company recorded a gain of \$0.1 million and \$5.9 million, respectively, associated with the repurchase of a portion of the Company's senior convertible debentures at a discount to carrying value.

The Company receives dividend income from certain investments held. Dividend income was \$4.0 million and \$17.0 million during the three and nine months ended September 30, 2010, respectively, a decrease of \$0.1 million and an increase of \$8.2 million compared to the same periods in 2009. Dividend income increased \$8.2 million during the nine months ended September 30, 2010 compared to the same period in 2009 primarily from the receipt of an \$8.3 million dividend from a private equity investment during first quarter 2010. The sale of approximately 12.1 million shares of Computershare Ltd. since July 1, 2009 is expected to have a negative impact on the Company's future dividend income.

The Company received a \$49.5 million cash dividend from a private equity investment on October 25, 2010. A portion of the dividend may qualify for the dividends received deduction which would result in a lower tax rate than the Federal statutory rate of 35%. The Company is not currently in a position to estimate the portion qualifying for the dividends received deduction.

Interest income was \$1.3 million and \$4.3 million during the three and nine months ended September 30, 2010, a decrease of \$0.2 million and an increase of \$0.1 million compared to the same periods in 2009.

Miscellaneous items include unrealized gains and losses on marketable securities designated as trading securities, program fees related to the Company's accounts receivable securitization program during 2009, realized foreign currency gains and losses, amortization of deferred non-operating gains and other non-operating items. Miscellaneous items was income of \$3.0 million and \$3.8 million during the three and nine months ended September 30, 2010 compared to income of \$5.2 million and \$4.2 million during the three and nine months ended September 30, 2009. The decrease in miscellaneous items for the three months ended September 30, 2010 is primarily from unrealized depreciation on marketable securities designated as trading (the effect of which is offset in Financial Services Segment as a decrease in costs and expenses), partially offset by the absence of accounts receivable securitization program costs which are now recorded in interest expense beginning January 1, 2010.

Table of Contents**Equity in earnings (losses) of unconsolidated affiliates**

The following table summarizes the Company's equity in earnings (losses) of unconsolidated affiliates (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
BFDS	\$ 4.0	\$ 2.2	\$ 11.7	\$ 9.0
IFDS, U.K.	3.1	2.0	9.6	5.8
IFDS, L.P.	1.5	2.1	5.5	4.7
Argus				(1.5)
Other	0.3	1.5	0.2	6.0
	\$ 8.9	\$ 7.8	\$ 27.0	\$ 24.0

DST's equity in earnings of unconsolidated affiliates increased \$1.1 million or 14.1% for the three months ended September 30, 2010 compared to the same period in 2009, primarily attributable to higher equity in earnings of BFDS and IFDS, U.K., partially offset by lower earnings of other unconsolidated affiliates and IFDS, L.P. DST's equity in earnings of unconsolidated affiliates increased \$3.0 million or 12.5% during the nine months ended September 30, 2010 compared to the same period in 2009, primarily attributable to higher equity in earnings of IFDS, U.K., BFDS and IFDS, L.P., partially offset by lower earnings of other unconsolidated affiliates.

DST's equity in BFDS earnings for the three and nine months ended September 30, 2010 increased \$1.8 million or 81.8% and \$2.7 million or 30.0% compared to the same periods in 2009. The increase during the three months ended September 30, 2010 is attributable to lower occupancy costs from vacating a facility in 2009, lower bank fees and improvements in operations. The increase during the nine months ended September 30, 2010, is from these same factors and from the release of a previously established income tax valuation allowance. BFDS derives investment earnings related to cash balances maintained on behalf of customers. Average daily balances invested by BFDS were \$0.9 billion during the three and nine months ended September 30, 2010, essentially unchanged as compared to the same periods in 2009. Average interest rates earned on the balances increased from 0.15% during the three months ended September 30, 2009 to 0.19% during the three months ended September 30, 2010. Average interest rates earned on the balances of 0.18% during the nine months ended September 30, 2009 were essentially unchanged compared to 0.17% during the nine months ended September 30, 2010. The aggregate effect of these fluctuations resulted in a minimal impact in interest earnings by BFDS during the three and nine months ended September 30, 2010.

DST's equity in earnings of IFDS, U.K. increased \$1.1 million and \$3.8 million during the three and nine months ended September 30, 2010 compared to the same periods in 2009. The increase in equity in earnings during the three and nine months ended September 30, 2010 is primarily attributable to higher levels of shareowner accounts serviced from both new and existing clients and improvements in operations. Accounts serviced by IFDS, U.K. were 7.0 million at September 30, 2010, unchanged from June 30, 2010 and an increase of 0.5 million accounts or 7.7% from September 30, 2009.

DST's equity in earnings of IFDS, L.P. (which includes IFDS Canada, Ireland and Luxembourg) decreased \$0.6 million and increased \$0.8 million during the three and nine months ended September 30, 2010 compared to the same periods in 2009. The decrease during the three months ended September 30, 2010 is primarily attributable to lower earnings at IFDS Ireland and Luxembourg. The increase during the nine months ended September 30, 2010 is primarily attributable to improvements in the Canadian operations. Accounts serviced by IFDS Canada were 10.7 million at September 30, 2010, a decrease of 0.1 million accounts or 0.9% from June 30, 2010 and an increase of 0.2 million accounts

or 1.9% from September 30, 2009.

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As previously announced, DST acquired the remaining 50% equity interest in Argus on March 31, 2009 and no longer records equity in earnings of Argus, but consolidates Argus' results into DST's consolidated financial statements.

Income taxes

The Company records income tax expense during interim periods based on its best estimate of the full year's tax rate. Certain items are given discrete period treatment and, as a result, the tax effects of such items are reported in full in the relevant interim period. The Company's income tax rate was 32.7% and 35.0% for the three and nine months ended September 30, 2010 compared to 35.8% and 30.0% for the three and nine months ended September 30, 2009. The decrease in the Company's income tax rate for the three months ended September 30, 2010 compared to the same period in 2009 is primarily related to the release of approximately \$2.3 million of valuation allowances against certain international deferred tax assets, which resulted from the acquisition of dsicmm.

The Company's income tax rate for the nine months ended September 30, 2010 included a benefit from a dividend received deduction on an \$8.3 million cash dividend received from a private equity investment. In addition, the release of the international valuation allowance mentioned above, lower levels of international operating losses requiring valuation allowances and higher benefits from foreign tax credits favorably impacted the Company's tax rate in 2010. During the nine months ended September 30, 2009, DST recorded a \$41.7 million gain on the purchase of the remaining 50% equity interest in Argus with no related income tax expense, reversed approximately \$0.9 million of deferred tax liabilities related to the elimination of deferred tax liabilities previously established for equity in earnings of Argus, and recorded an income tax benefit of approximately \$5.7 million resulting from a reduction in income tax liabilities principally associated with the completion of an IRS examination in February 2009 for the tax years ended December 31, 2002 through 2005.

Excluding the effects of discrete period items and the private equity investment cash dividend mentioned above, the Company expects its tax rate to be approximately 36.0% for the remainder of 2010 but this rate will likely vary depending on the 2010 sources of taxable income (e.g. domestic consolidated, international and / or joint venture). The full year 2010 tax rate can be affected as a result of variances among the estimates and amounts of full year sources of taxable income, the realization of tax credits (e.g., historic rehabilitation, research and experimentation, foreign tax and state incentive), adjustments which may arise from the resolution of tax matters under review and the Company's assessment of its liability for uncertain tax positions.

Business Segment Comparisons

FINANCIAL SERVICES SEGMENT

Revenues

Financial Services Segment total revenues for the three and nine months ended September 30, 2010 were \$301.9 million and \$899.2 million, respectively, an increase of \$14.0 million or 4.9% and \$25.9 million or 3.0% compared to the same periods in 2009. Financial Services Segment operating revenues for the three months ended September 30, 2010 were \$290.4 million, an increase of \$14.1 million or 5.1% compared to the

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same period in 2009. As previously announced, a client with approximately 5.0 million subaccounts terminated its processing contract in connection with a corporate merger and converted to a non-DST subaccounting platform during third quarter 2010. DST received a termination payment of approximately \$10.4 million (\$9.1 million was recorded in Financial Services and \$1.3 million was recorded in Output Solutions) and incurred approximately \$1.6 million of costs in connection with the contract termination, resulting in a \$8.8 million net pretax gain associated with this event. Absent this contract termination payment of \$9.1 million, Financial Services Segment operating revenues for the three months ended September 30, 2010 increased \$5.0 million or 1.8% compared to the same period in 2009. On this basis, the increase in Financial Services operating revenues is attributable to higher revenues at DST Global Solutions and Argus, partially offset by lower revenues at DST Health Solutions.

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Revenues of DST Global Solutions increased from higher professional services and changes in foreign currency exchange rates, which increased operating revenues by approximately \$1.3 million, partially offset by lower software license revenues. Argus revenues increased due to higher pharmacy claims related services. DST Health Solutions experienced lower demand for professional services and lower volumes of transaction processing. U.S. Investment Recordkeeping Solutions operating revenues during third quarter 2010 were essentially unchanged as increased revenues from higher retirement participant recordkeeping services, higher volume of subaccounts serviced and increased distribution support solutions volumes were offset by decreased shareowner processing revenues from lower levels of registered accounts.

Financial Services Segment operating revenues for the nine months ended September 30, 2010 were \$864.0 million, an increase of \$32.3 million or 3.9% compared to the same period in 2009. Absent the \$9.1 million client contract termination payment mentioned above and \$26.0 million of net incremental operating revenues resulting from the acquisition and consolidation of Argus on March 31, 2009, Financial Services operating revenues for the nine months ended September 30, 2010 decreased \$2.8 million or 0.3% compared to the same period in 2009. On this basis, the decrease in Financial Services operating revenues is attributable to lower DST Health Solutions revenues, partially offset by higher Global Solutions and Argus revenues. This operating revenue decrease was partially offset by changes in foreign currency exchange rates which increased operating revenues by approximately \$9.2 million. U.S. Investment Recordkeeping Solutions operating revenues during the nine months ended September 30, 2010 were slightly higher than for the same period in 2009. Increased revenues from higher retirement participant recordkeeping services, higher volume of subaccounts serviced and increased distribution support solutions volumes were offset by decreased shareowner processing revenues from lower levels of registered accounts.

U.S. operating revenues for the three months ended September 30, 2010 were \$263.0 million, an increase of \$12.0 million or 4.8% compared to the same period in 2009. Absent the \$9.1 million client contract termination payment mentioned above, U.S. operating revenues for the three months ended September 30, 2010 increased \$2.9 million or 1.2% compared to the same period in 2009. On this basis, the increase during the three months ended September 30, 2010 is attributable to higher revenues at Argus due to higher pharmacy claims related services, partially offset by lower volumes of DST Health Solutions professional service revenues. U.S. operating revenues for the nine months ended September 30, 2010 were \$779.1 million, an increase of \$21.5 million or 2.8% compared to the same period in 2009. Absent \$26.0 million net incremental increase in U.S. operating revenues resulting from the consolidation of Argus and the \$9.1 million client contract termination payment, as mentioned above, U.S. operating revenues decreased \$13.6 million or 1.8% compared to the same period in 2009. On this basis, the decrease during the nine months ended September 30, 2010 is attributable to lower DST Health Solutions revenues, partially offset by higher Argus revenues. U.S. Investment Recordkeeping Solutions operating revenues during the nine months ended September 30, 2010 were slightly higher than for the same period in 2009.

International operating revenues for the three and nine months ended September 30, 2010 were \$27.4 million and \$84.9 million, an increase of \$2.1 million or 8.3% and an increase of \$10.8 million or 14.6% compared to the same periods in 2009. International operating revenues for the three months ended September 30, 2010 increased primarily from the change in foreign currency exchange rates between the U.S. Dollar and other foreign currencies of approximately \$1.3 million compared to the same period in 2009 and from higher professional services.

Financial Services Segment software license fee revenues are derived principally from AWD (business process management - BPM), DST Global Solutions (investment management) and DST Health Solutions (medical claims processing). Operating revenues include approximately \$9.5 million and \$31.8 million of software license fee revenues for the three and nine months ended September 30, 2010, a decrease of \$0.9 million or 8.7% and \$0.1 million or 0.3% compared to the same periods in 2009. The decrease during the three months ended September 30, 2010 is primarily due to lower investment management and medical claims license fee revenue. While license revenues are not a significant percentage of DST's total operations, they can significantly impact earnings in the period in which they are recognized. Revenues and operating results from individual license sales depend heavily on the timing, size and nature of the contract.

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Costs and expenses

Financial Services Segment costs and expenses (including OOP costs) were \$209.6 million and \$637.9 million during the three and nine months ended September 30, 2010, respectively, a decrease of \$1.8 million or 0.9% and an increase of \$5.6 million or 0.9% compared to the same periods in 2009. Costs and expenses in the Financial Services Segment are primarily comprised of compensation and benefits costs, but also include reimbursable operating expenses and other costs. Reimbursable operating expenses included in costs and expenses were \$11.5 million and \$35.2 million during the three and nine months ended September 30, 2010, respectively, a decrease of \$0.1 million and \$6.4 million compared to the same periods in 2009. Excluding reimbursable operating expenses, expenses incurred in connection with terminating a client contract mentioned above of \$1.6 million and termination benefit expenses of \$0.7 million related to a reduction in force incurred during the three months ended September 30, 2010, costs and expenses decreased \$4.0 million or 2.0% during the three months ended September 30, 2010 to \$195.8 million. On this basis, the decrease in costs and expenses is attributable to lower compensation and benefit related costs from lower staffing levels, lower deferred compensation costs of \$2.1 million (the effect of which is offset in other non-operating income) partially offset by higher costs from foreign currency exchange effects between the U.S. Dollar and other currencies of approximately \$1.2 million, higher welfare benefit costs and new product development costs.

Excluding reimbursable operating expenses, costs and expenses of Argus during the three months ended March 31, 2010 of \$27.6 million, expenses incurred in connection with terminating a client contract mentioned above of \$1.6 million and termination benefit expenses of \$12.1 million related to a reduction in force, costs and expenses decreased \$29.3 million or 5.0% during the nine months ended September 30, 2010 to \$561.4 million. On this basis, the decrease in costs and expenses is attributable to lower compensation and benefit related costs from lower staffing levels, lower deferred compensation costs of \$4.1 million (the effect of which is offset in other non-operating income), partially offset by higher costs from foreign currency exchange effects between the U.S. Dollar and other currencies of approximately \$8.1 million.

Depreciation and amortization

Financial Services Segment depreciation and amortization costs for the three and nine months ended September 30, 2010 decreased \$1.4 million or 6.7% as compared to the three months ended September 30, 2009 and increased \$1.2 million or 2.1% as compared to the nine months ended September 30, 2009. The decrease during the three months ended September 30, 2010 is attributable to lower depreciation from certain assets becoming fully depreciated and the Company's use of accelerated depreciation methods, partially offset by increased capitalized software activity. The increase in depreciation and amortization during the nine months ended September 30, 2010 is primarily related to higher purchase accounting amortization expense from the consolidation of Argus on March 31, 2009, partially offset by the Company's use of accelerated depreciation methods.

Income from operations

Financial Services Segment income from operations for the three and nine months ended September 30, 2010 was \$72.8 million and \$202.6 million, respectively, an increase of \$17.2 million or 30.9% and \$19.1 million or 10.4% compared to the same periods in 2009. Excluding the impact of a contract termination payment of \$9.1 million, costs associated with this contract termination of \$1.6 million and termination benefit expenses from a reduction in force of \$0.7 million, income from operations increased \$10.4 million to \$66.0 million during the three months ended September 30, 2010 as compared to the same period in 2009. On this basis, the increase in Financial Services income from operations is attributable to higher revenues and lower personnel costs, including \$2.1 million of decreased deferred compensation costs mentioned above. Excluding the impact of the termination benefit expenses of \$12.1 million, contract termination revenues of \$9.1 million, costs associated with this contract termination of \$1.6 million and termination benefit expenses from a reduction in force, income from operations increased \$23.7

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million to \$207.2 million during the nine months ended September 30, 2010 as compared to the same period in 2009. On this basis, Financial Services income from operations increased from higher revenues and lower operating expenses, including \$4.1 million of decreased deferred compensation costs mentioned above.

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Financial Services Segment Account Statistics

The following table summarizes mutual fund shareowner accounts serviced (in millions):

	September 30, 2010	June 30, 2010	December 31, 2009	September 30, 2009
Registered accounts:				
Non tax-advantaged	57.3	60.8	63.6	63.4
Tax-advantaged	45.7	46.5	46.3	46.3
	103.0	107.3	109.9	109.7