

GARTNER INC
Form 10-Q
July 31, 2007

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

(Mark One)

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

For the quarterly period ended June 30, 2007

OR

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

For the transition period from to

Commission File Number 1-14443

Gartner, Inc.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

04-3099750
(I.R.S. Employer
Identification Number)

P.O. Box 10212
56 Top Gallant Road
Stamford, CT
(Address of principal executive offices)

06902-7700
(Zip Code)

Registrant's telephone number, including area code: (203) 316-1111

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large Accelerated Filer Accelerated Filer Non-accelerated Filer

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

As of July 24, 2007, 105,517,056 shares of the registrant's common shares were outstanding.

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****GARTNER, INC.**Condensed Consolidated Balance Sheets
(Unaudited, in thousands)

	June 30, 2007	December 31, 2006
Assets		
Current assets:		
Cash and cash equivalents	\$ 102,838	\$ 67,801
Fees receivable, net	303,508	328,383
Deferred commissions	43,520	46,822
Prepaid expenses and other current assets	65,792	41,027
Total current assets	515,658	484,033
Property, equipment and leasehold improvements, net	60,653	59,715
Goodwill	410,956	408,545
Intangible assets, net	4,613	5,978
Other assets	87,625	81,522
Total Assets	\$ 1,079,505	\$ 1,039,793
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 177,905	\$ 208,002
Deferred revenues	377,183	375,881
Current portion of long-term debt	193,500	220,000
Total current liabilities	748,588	803,883
Long-term debt	166,500	150,000
Other liabilities	83,956	59,592
Total Liabilities	999,044	1,013,475
Stockholders Equity		
Preferred stock		
Common stock	78	78
Additional paid-in capital	539,506	544,686
Unearned compensation, net	(636)	(2,208)
Accumulated other comprehensive income, net	18,098	13,097
Accumulated earnings	271,244	249,004
Treasury stock, at cost	(747,829)	(778,339)
Total Stockholders Equity	80,461	26,318
Total Liabilities and Stockholders Equity	\$ 1,079,505	\$ 1,039,793

See the accompanying notes to the condensed consolidated financial statements.

Table of Contents**GARTNER, INC.**Condensed Consolidated Statements of Operations
(Unaudited, in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Revenues:				
Research	\$ 163,753	\$ 138,321	\$ 322,553	\$ 275,413
Consulting	83,555	83,663	159,822	159,556
Events	53,005	58,599	79,932	73,094
Other	3,178	3,510	5,381	6,959
Total revenues	303,491	284,093	567,688	515,022
Costs and expenses:				
Cost of services and product development	144,211	137,283	267,924	242,632
Selling, general and administrative	120,523	106,701	236,269	206,168
Depreciation	6,012	6,098	11,747	11,758
Amortization of intangibles	596	3,416	1,125	6,799
META integration charges				1,450
Other charges	9,084		9,084	
Total costs and expenses	280,426	253,498	526,149	468,807
Operating income	23,065	30,595	41,539	46,215
Interest expense, net	(5,398)	(4,479)	(11,661)	(8,842)
Other income (expense), net	1,814	173	1,776	(521)
Income before income taxes	19,481	26,289	31,654	36,852
Provision for income taxes	5,433	8,045	9,414	10,838
Net income	\$ 14,048	\$ 18,244	\$ 22,240	\$ 26,014
Income per common share:				
Basic	\$ 0.13	\$ 0.16	\$ 0.21	\$ 0.23
Diluted	\$ 0.13	\$ 0.16	\$ 0.20	\$ 0.22
Weighted average shares outstanding:				
Basic	104,259	113,525	103,890	113,646
Diluted	109,571	115,743	108,941	115,911

See the accompanying notes to the condensed consolidated financial statements.

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GARTNER, INC.
Condensed Consolidated Statements of Cash Flows
(Unaudited, in thousands)

	Six Months Ended June 30,	
	2007	2006
<i>Operating activities:</i>		
Net income:	\$ 22,240	\$ 26,014
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of intangibles	12,872	18,557
Stock-based compensation expense	13,407	6,997
Excess tax benefits from stock-based compensation	(13,726)	(3,653)
Deferred taxes	(349)	(2,302)
Amortization and writeoff of debt issue costs	914	403
Changes in assets and liabilities:		
Fees receivable, net	28,012	32,829
Deferred commissions	3,690	12,278
Prepaid expenses and other current assets	(22,955)	(413)
Other assets	(6,540)	(572)
Deferred revenues	(3,030)	1,568
Accounts payable and accrued liabilities	9,158	(58,727)
<i>Cash provided by operating activities</i>	43,693	32,979
<i>Investing activities:</i>		
Additions to property, equipment and leasehold improvements	(12,430)	(7,978)
Other investing activities, net	9	(209)
<i>Cash used in investing activities</i>	(12,421)	(8,187)
<i>Financing activities:</i>		
Proceeds from interest rate swap termination	1,167	
Proceeds from stock issued for stock plans	27,522	22,073
Proceeds from debt issuance	405,000	
Payments for debt issuance costs	(1,257)	
Payments on debt	(415,000)	(16,666)
Purchases of treasury stock	(29,690)	(37,025)
Excess tax benefits from stock-based compensation	13,726	3,653
<i>Cash provided (used) in financing activities</i>	1,468	(27,965)
Net increase (decrease) in cash and cash equivalents	32,740	(3,173)
Effects of exchange rates on cash and cash equivalents	2,297	1,958
Cash and cash equivalents, beginning of period	67,801	70,282
Cash and cash equivalents, end of period	\$ 102,838	\$ 69,067

See the accompanying notes to the condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1 Basis of Presentation

These interim condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and should be read in conjunction with the consolidated financial statements and related notes of Gartner, Inc. (Gartner or the Company) filed in its Annual Report on Form 10-K for the year ended December 31, 2006.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of operating revenues and expenses. These estimates are based on management's knowledge and judgments. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of financial position, results of operations and cash flows at the dates and for the periods presented have been included. The results of operations for the three and six months ended June 30, 2007 may not be indicative of the results of operations for the remainder of 2007. Certain prior year amounts have been reclassified to conform to the current year presentation. Sales tax collected from customers remitted to governmental authorities is presented on a net basis in the Condensed Consolidated Statements of Operations.

Note 2 Comprehensive Income

The components of comprehensive income, net of tax effect, for the three and six months ended June 30, 2007 and 2006 are as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2007	2006	2007	2006
Net income	\$ 14,048	\$ 18,244	\$ 22,240	\$ 26,014
Other comprehensive income, net of tax:				
Foreign currency translation adjustments	2,883	2,935	3,648	3,207
Unrealized gain on interest rate swap	1,469	860	384	2,117
Realized gain on interest rate swap (a)	(128)		905	
Amortization of pension unrealized loss	32		64	
Other comprehensive income	4,256	3,795	5,001	5,324
Comprehensive income	\$ 18,304	\$ 22,039	\$ 27,241	\$ 31,338

(a) The six months ended June 30, 2007 is net of approximately \$0.2 million reclassified to earnings.

Note 3 Computations of Income per Share of Common Stock

The following table sets forth the reconciliation of the basic and diluted income per share (in thousands, except per share data):

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2007	2006	2007	2006

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Numerator:

Net income used for calculating basic and diluted income per share	\$ 14,048	\$ 18,244	\$ 22,240	\$ 26,014
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Denominator:

Weighted average number of common shares used in the calculation of basic income per share	104,259	113,525	103,890	113,646
Common stock equivalents associated with stock-based compensation plans	5,312	2,218	5,051	2,265
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	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2007	2006	2007	2006
Shares used in the calculation of diluted income per share	109,571	115,743	108,941	115,911
Basic income per share	\$ 0.13	\$ 0.16	\$ 0.21	\$ 0.23
Diluted income per share	\$ 0.13	\$ 0.16	\$ 0.20	\$ 0.22

For the three months ended June 30, 2007 and 2006, 0.6 million and 2.2 million options and stock appreciation rights, respectively, were not included in the computation of diluted income per share because the effect would have been anti-dilutive.

For the six months ended June 30, 2007 and 2006, 0.5 million and 2.0 million options and stock appreciation rights, respectively, were not included in the computation of diluted income per share because the effect would have been anti-dilutive.

Note 4 Stock-Based Compensation

The Company grants stock-based compensation awards as an incentive for employees and directors to contribute to the Company's long-term success. The Company's awards include stock options, stock-settled stock appreciation rights, restricted stock, service- and performance-based restricted stock units, and common stock equivalents.

The Company accounts for stock-based compensation in accordance with Statement of Financial Accounting Standards 123(R), Share-Based Payment (SFAS No. 123(R)), as interpreted by SEC Staff Accounting Bulletin No. 107 (SAB No. 107). Under SFAS No. 123(R), stock-based compensation expense is based on the fair value of the award on the date of grant, which is recognized over the related service period, net of estimated forfeitures. The service period is the period over which the related service is performed, which is generally the same as the vesting period. All of the Company's stock-based compensation awards are classified as equity awards in accordance with SFAS No. 123(R). The Company recognized the following amounts of stock-based compensation expense under SFAS No. 123(R) in the Condensed Consolidated Statement of Operations (in thousands):

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2007	2006	2007	2006
Amount recorded in:				
Costs of services and product development expense	\$ 3,500	\$ 2,600	\$ 6,100	\$ 4,000
Selling, general, and administrative expense	4,300	1,900	7,300	3,000
Total stock-based compensation expense	\$ 7,800	\$ 4,500	\$ 13,400	\$ 7,000

As of June 30, 2007, the Company had \$50.5 million of total unrecognized stock-based compensation cost, which is expected to be recognized as stock-based compensation expense over the remaining weighted-average service period of approximately 2.6 years. For the six months ended June 30, 2007, excess tax benefits realized from the exercise of stock-based compensation awards was \$13.7 million, compared to \$3.7 million in the prior year period. Currently the Company issues treasury shares upon the exercise or settlement of stock-based compensation awards.

Stock Options and Stock Appreciation Rights

A summary of the changes in stock options outstanding during the six months ended June 30, 2007 follows:

Weighted

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	Options in millions	Weighted Average Exercise Price	Average Remaining Contractual Term
Outstanding at December 31, 2006	12.8	\$ 11.10	5.17 years
Granted			
Forfeited or expired	(0.1)	11.41	nm
Exercised (1)	(2.2)	11.49	nm
Outstanding at June 30, 2007 (2)	10.5	\$ 11.01	4.84 years
Vested and exercisable at June 30, 2007 (2)	8.8	\$ 10.99	4.70 years

nm=not meaningful

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- (1) The Company received approximately \$26.1 million in cash from stock option exercises in the first six months of 2007. Options exercised during the first six months of 2007 had an intrinsic value of approximately \$30.0 million
- (2) At June 30, 2007, options outstanding and options vested and exercisable had aggregate intrinsic values of \$141.9 million and \$120.1 million, respectively.

A summary of the changes in stock-settled stock appreciation rights (SARs) outstanding during the six months ended June 30, 2007 follows:

	SARs in millions	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value	Weighted Average Remaining Contractual Term
Outstanding at December 31, 2006	1.2	\$ 14.48	\$6.02	6.38 years
Granted (1)	0.6	21.93	8.00	6.99 years
Forfeited or expired				
Exercised				
SARs outstanding at June 30, 2007 (2)	1.8	\$ 17.07	\$6.71	6.14 years
Vested and exercisable at June 30, 2007	0.3	\$ 14.44	\$6.01	5.87 years

- (1) SARs generally vest ratably over a four-year service period and expire in seven years.
- (2) At June 30, 2007, SARs outstanding had an aggregate intrinsic value of \$13.6 million, and SARs vested and exercisable had an intrinsic value of \$2.9 million.

The fair value of the Company's stock options and SARs was estimated on the date of grant using the Black-Scholes-Merton valuation model with the weighted-average assumptions in the table below:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006 (1)	2007	2006
Expected dividend yield (2)	0%		0%	0%
Expected stock price volatility (3)	30%		33%	40%
Risk-free interest rate (4)	4.6%		4.7%	4.7%
Expected life in years (5)	4.5		4.7	4.8

- (1) No awards were made in this period.
- (2) The dividend yield assumption is based on the history and expectation of the Company's dividend payouts. Historically, Gartner has not paid dividends on its common

stock.

- (3) Expected stock price volatility was based on both historical Gartner common stock prices and implied volatility from publicly traded options in Gartner common stock.
- (4) The risk-free interest rate is based on the yield of a U.S. treasury bond with a similar maturity of the expected life of the award.
- (5) The expected life in years was based on the simplified calculation provided for in SAB No. 107. The simplified method determines the expected life in years based on the vesting period and contractual terms as set forth when the award is made.

Restricted Stock, Restricted Stock Units, and Common Stock Equivalents

The fair value of restricted stock, restricted stock units (RSUs), and common stock equivalents (CSEs) is determined on the date of grant based on the market price of the Company's common stock. The fair value of these awards is recognized as compensation expense as follows: (i) restricted stock awards generally vest based on the achievement of a market condition and are expensed on a straight-line basis over approximately three years; (ii) service-based RSUs vest ratably over four years and are expensed on a straight-line basis over four years; (iii) performance-based RSUs are subject to both performance and service conditions, vest

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ratably over four years, and are expensed on an accelerated basis as required by SFAS No. 123(R); and (iv) CSEs vest immediately and are recorded as expense on the date of grant.

A summary of the changes in restricted stock, restricted stock units, and common stock equivalents during the six months ended June 30, 2007, is presented in the table below:

	Restricted Stock	Weighted- Average Grant Date Fair Value	Restricted Stock Units (RSUs)	Weighted- Average Grant Date Fair Value	Common Stock Equivalents (CSEs)	Weighted- Average Grant Date Fair Value
Nonvested at December 31, 2006	511,000	\$8.81	1,521,620	\$14.13		\$
Granted (1), (2)						
<u>Exchange Act</u>	1					
<u>Incentive Stock Option</u>	5					
<u>Incumbent Board</u>	10					
<u>Non-Employee Directors</u>	2					
<u>Nonqualified Stock Option</u>	3					
<u>Outstanding Common Stock</u>	9					
<u>Outstanding Voting Securities</u>	9					
<u>Performance Criteria</u>	7					
<u>Performance Period</u>	6					
<u>Performance Stock</u>	6					
<u>Performance Units</u>	6					
<u>Performance-Based Exception</u>	6					
<u>Person</u>	10					
<u>Plan</u>	1					
<u>Prior Plans</u>	1					
<u>SARs</u>	5					
<u>Schwab</u>	1					
<u>Section 409A</u>	11					