

# FINAL TRANSCRIPT

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## **IMN - Q3 2011 Imation Corp Earnings Conference Call**

**Event Date/Time: Oct. 25. 2011 / 2:00PM GMT**



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## CORPORATE PARTICIPANTS

**Scott Robinson**

*Imation Corporation - VP, Corporate Controller and CAO*

**Mark Lucas**

*Imation Corporation - President and CEO*

**Paul Zeller**

*Imation Corporation - VP and CFO*

## CONFERENCE CALL PARTICIPANTS

**Mark Miller**

*Noble Financial Markets - Analyst*

**Rich Rubin**

*Hawkeye Capital - Analyst*

**Chuck Murphy**

*Sidoti & Co. - Analyst*

## PRESENTATION

**Operator**

Good day, ladies and gentlemen, and welcome to the Imation third-quarter analyst conference call. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session and instructions will follow at that time. (Operator Instructions). As a reminder, this conference is being recorded.

I would now like to turn the conference over to Scott Robinson. You may begin.

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**Scott Robinson** - *Imation Corporation - VP, Corporate Controller and CAO*

Thank you, Latoya. Good morning, everyone, and welcome to our quarter three 2011 earnings conference call. I am delighted to be your host for today's call, where you will be hearing from our CEO, Mark Lucas, and our CFO, Paul Zeller. On today's call, we will review our third-quarter results and also provide information regarding the progress we are making in regard to our strategy.

Before I turn the call over to Mark and Paul for their comments followed by your questions, I want to remind everyone that certain information discussed on this call that does not relate to historical information may be deemed to be constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are subject to risks and uncertainties that could cause actual results to differ materially from any projected results.

Risk factors that could cause results to differ are outlined in the press release issued today as well as our filings with the SEC.

With that, I'd like to turn the call over to Mark Lucas, Imation's CEO.

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**Mark Lucas** - *Imation Corporation - President and CEO*

Thank you, Scott, and good morning, everyone. In our call today I would like to update you on Imation's progress as we continue our strategic transformation to a global technology company focused on growth opportunities in data storage, protection, and connectivity.

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Let's begin with a review of revenue. As we stated, our goal is to return to revenue growth by the end of 2012. We continued to deliver growth in our secure and scalable products during the quarter, but we have not yet hit the inflection point where these revenues will offset declines in our traditional storage area.

Our RDX line for example grew 25%, driven by increasing adoption by OEMs and end users. We recently completed an agreement with OEM partner Quantum to supply its RDX 8000 hard disk storage libraries. While our RTX growth is still on a small base, we are pleased by the traction we continue to see and expect continued growth in our scalable products category.

In our secure products, we have had several key wins with our Defender flash drive line in government and medical markets and expect mobile security to be a growth area in the future. I will talk more about this in a few minutes.

In our audio and video information products, formerly called consumer electronics products, we saw a 12% growth in accessories with several new retail placements for our XtremeMac line. Excluding rationalized video products, other audio and video information products grew almost 8%.

Just to note that with this name change to audio and video information or AVI, there is no change to the definition of products within the category. We believe that this new characterization better articulates our focus on products that improve the consumer's experience of how they consume and interact with both audio and video digital content.

Now let's shift to a discussion of gross margins, where we are pleased with the steady progress we are making. In our ABI category, gross margins continue to improve from previously low single digits. In secure and scalable storage, which are growth areas for our Company, our margins improved and were more than 15% in the quarter. And in traditional storage, our margins held steady. Paul will provide more detail on each of our product categories in just a few minutes.

Obviously we are in a strategic transformation and we continue to execute on the strategic direction outlined earlier this year including key technology investments in secure and scalable storage.

Let's talk specifically about secure storage. You will recall that Imation first entered the high-security data storage and device management market in 2010 with the launch of our Defender line of secure hardware and software management products. In March of this year, we acquired ENCRYPTX, a leader in encryption and software security solutions. And in June, we acquired MXI Security, adding MXI technologies and solutions for device security including the Stealth Zone platform for secure computing environments.

Last month we announced our acquisition of IronKey's security hardware business, which includes USB storage technologies and products that support cloud-based management. At the same time, we announced a new strategic partnership with IronKey for online services. We have completed these agreements this month, enabling Imation to expand in the fast-growing USB device market.

With these acquisitions, we have now created an Imation mobile security team headquartered in Sunnyvale, California, integrating with Imation's international locations serving customers in more than 100 countries. This focus team includes many of the top technology sales and marketing personnel in the mobile security industry. We have created a significant technology leadership position that will deliver a solution set for securing mobile data and mobile workplaces.

We now have added a whole new set of new enterprise and government customers to our already significant customer base worldwide. We look to the secure storage area for future growth and strong gross margin performance.

Another area of strategic investment is in our scalable storage area where we are creating a tiered storage platform of data archive and data protection products with a focus on small and medium-sized businesses. In August, Imation acquired certain assets of ProStor, including InfiniVault technology and products, because we recognized the need to add a compelling tiered storage architecture to our existing portfolio of backup and archiving products.

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InfiniVault combines multiple media options including fixed rate disk and RDX removable hard drive disks in a single storage environments that will retrieve, retain, protect, and archive digital content. InfiniVault software will enable Imation to deliver future tiered storage solutions using RDX and other hard disk optical magnetic and solid-state storage. This software helps strengthen the Imation RDX portfolio and InfiniVault offering.

Our team just returned from the storage networking world show where we unveiled our newest scalable storage platform, which we will be launching in the coming months. Response from OEMs, VAR partners, and end-users to our new line has been very positive. Imation has the storage expertise and global reach to be the trusted storage adviser for SMB's two large enterprises and we are excited about the potential for our new scalable storage line.

In addition to the technology investments we are making, we continue to add skills to our global team. Our acquisitions have brought new team members with specialized skills in product and software development, marketing, and sales for secure and scalable storage. Additionally, we've added sales management with deep industry experience of bringing products to market through value-added resellers and distributor channels which are a critical enabler to reaching our SMB customers.

In our AVI area, we are pleased to have recently added two experienced consumer electronic industry leaders who will continue to drive improvements in our business.

Our Imation team worldwide is energized by the progress we are making on our strategy and by the infusion of new skill sets in key areas. We are confident we are implementing the right strategies and building an industry-leading team to drive our transformation forward.

Now I would like to turn the call over to Paul, who will provide more financial detail on the quarter. Paul?

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**Paul Zeller** - *Imation Corporation - VP and CFO*

Thanks, Mark, and good morning, everyone. As you just heard, Q3 was a bit of a mixed quarter. There were some positive signs such as growth we saw in certain categories like RDX and accessories and continuing improvements in our gross margin profile especially in our growth categories of secure and scalable storage and audio and video information.

On the downside, we continued to see cost pressures in our optical business, though we were able to offset this in Q3 through both a levy benefit in Europe as well as price increases to our customers. In addition, our US consumer business was weak in the quarter especially in retail.

Let me get into some of the details. In terms of revenue, we had \$208.6 million in the quarter. That's down 9.8% compared to Q3 last year. That's a similar rate of decline as we saw last quarter. This decline includes a currency benefit of approximately 4%.

Traditional storage revenues declined 11.7% coming from 14% decline in optical revenues and an 8% decline in magnetic tape. In optical, which now represents about 40% of our worldwide revenues, we've seen our decline rate moderate from the upper teens rates we saw last year and early this year to a 14% decline rate for this quarter. We do continue to believe this category will decline going forward.

In magnetic tape, which represents about 25% of revenues, we have seen our decline rate moderate to the single-digit range this year compared to the teens last year.

We have stated that we need to slow our overall decline rate as a Company on our way to returning to growth by the end of next year. We are doing this through a focus on driving growth in secure and scalable storage and in audio and video information, and we are doing that in order to offset the declines coming from our traditional storage category, which as you know is optical and tape media.



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We are seeing progress towards this objective with our total revenue decline rate moderating to under 10% and that is better than what we experienced last year. Having said that, and while this is progress, we clearly need more over time. To achieve our goals, we need to see accelerating growth from our growth product categories and I will address our progress in these areas.

First is secure and scalable storage. We grew it 3% in the third quarter despite some further rationalization of low margin external hard disk business. If we exclude the declines in non-differentiated HDD products, secure and scalable storage grew about 7%. Our best growth rate, as Mark mentioned, was in RDX at about 25% and we've seen 25% to 35% growth in that category all year long.

We are focused on driving growth in this category both organically and inorganically. As Mark mentioned, we began seeing the benefits of our MXI acquisition in the quarter and we completed the acquisition of IronKey just after quarter end and expect to see benefits from this acquisition as we go forward.

Our audio and video information revenues were down 13% in the quarter. That entire decline was driven by video products and legacy optical storage cases. Both of those declines were expected.

In video, we have intentionally exited this low-margin category over the last year. Revenues are now just about zero.

In terms of optical cases, we are seeing significant declines in this mature category as we expected. If we exclude video, ADI grew almost 8% and as I will get into in more detail shortly, this growth was focused on higher margin products which benefited our gross margins. In fact, the difference between the low-margin video products we have exited and the growing products like accessories can be 15 to 20 points.

From a segment standpoint, our Americas segment revenue declined about 20% versus Q3 last year. This was driven by continuing declines in traditional storage as well as the video product rationalization I just mentioned.

Europe is stabilizing and it was down just 5% versus last year compared to decline rates of 20% to 30% in prior quarters. Currency was a nice contributor in Europe this quarter.

North and South Asia revenues both increased for the second quarter in a row. North Asia increased 3.9% and South Asia 8.3%. We are pleased with this trend and currencies also benefited our Asia comparisons.

So stepping back and looking at Q3 revenue performance, traditional storage continued to decline as expected. Optical in the mid teens, tape in the single digits. We continued intentional product rationalization actions, most notably in video and external hard disks. That impacted our year-over-year revenue comparisons, but helped improve our gross margin percent.

We saw some positive signs in terms of new product growth. We need more, but it was good to see momentum building in key products like RDX and [CE] accessories. Currency has become a nice positive with the weakening of the dollar and we anticipate our acquisitions to add more revenue as we move forward.

In terms of gross margins, they came in at 18.5% to sales in the quarter. That's up 2.3 percentage points from last year's third quarter. If we look at it by category, traditional storage margins for the quarter were at 19.9%, up 1.8 percentage points from Q3 last year as driven by several factors.

As we signaled last quarter, we saw margin pressure in optical as our supplier costs were increasing and that continued this quarter. Both polycarbonate and silver, which are important raw materials for the manufacturing process, had seen marked increases in the past. Offsetting the impact from these supplier cost increases, we received a \$7.2 million benefit from the reversal of certain optical levy accruals in Europe.

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Though we anticipate these levy benefits may continue in the coming quarters, we also expect supplier cost pressures to continue. In light of this, we've been instituting price increases with our customers and are looking at ways to mitigate the cost increases.

In terms of magnetic tape margins, they were down slightly during the quarter due to mix changes. Secure and scalable storage gross margin was at 15.6%, up over 5 points from last year's third quarter. Though still on a small base, we are definitely pleased with the result. This category is being benefited by a very strong 45% plus gross margin we are delivering in our secure storage business. That's the Imation Defender as well as the impact of the MXI acquisition. RDX margins were also strong and up from both last quarter and last year.

In audio and video information, our margins were 15% with our strongest margins continuing to come from the accessories side of the business, where we again saw margins of over 20%. These margins improvements in our growth categories are encouraging and are core to our continuing transformation. This is the first quarter where we've seen 15% plus gross margins in both of our growth categories. We will continue to focus on delivering products with better than average gross margins moving forward.

Also in Q3, we sold some nonstrategic intellectual property which contributed \$2.4 million to our gross margins. That's about 0.8% to sales impact on gross margin.

Our RD&E expenses, research development and engineering, totaled \$5.3 million in the quarter. That's up \$1 million from a year ago and reflects our planned increased investment in technical skills in support of our strategy including recent acquisitions. Our RD&E headcount has increased by 60 in 2011 and that includes technical skills acquired with MXI.

Selling, general, and admin expenses totaled \$52.7 million, up \$3.4 million from last year driven by our acquisitions and incremental organic investments.

We recorded a \$2 million litigation charge to settle a long-standing supply agreement with ARC. We believe this was a prudent settlement in light of the litigation costs that would have been incurred to defend our position.

We recorded \$5.5 million in special charges in the quarter. These related mainly to our previously announced restructuring program and a pension settlement charge.

Our operative loss for the quarter including those charges was \$8.3 million. Excluding those charges, it was an operating loss of \$800,000. We had \$9.3 million in depreciation and amortization and an EBITDA of \$8 million excluding charges.

Nonoperating expenses increased to \$3.7 million for the third quarter. That compares to \$900,000 third quarter last year and \$2.7 million last quarter. Currencies were particularly volatile during the quarter, leading to higher than normal currency losses.

Our income tax provision for the quarter was \$2.1 million on a pretax loss of \$12 million. We maintain a valuation allowance related to US deferred tax assets and therefore were not able to report a tax benefit for our US losses. The provision represents tax expense on income outside the US.

So on a per-share basis, we recorded a loss of \$0.38 and if you exclude the various restructuring and litigation charges I mentioned, we had a loss per share of \$0.18.

We ended September with \$232 million of cash and equivalents. That's down \$25 million from last quarter. A number of factors in the quarter in addition to typical operating cash flows and those included in \$8.3 million payment related to the 2009 Philips settlement and share repurchases which totaled \$3 million in the quarter.

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So in summary, we are seeing continued progress as we implement our strategy. The growth we're seeing in certain key categories is encouraging, as is the continuing improvements quarter by quarter in our margins and our growth categories. We remain committed to and confident in our strategy and in our long-term financial goals of returning the Company to growth by the end of next year and continuing improvements over time in our gross margins.

With that, we would be pleased to take your questions. Thank you.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Mark Miller, Noble Capital.

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### Mark Miller - Noble Financial Markets - Analyst

Good morning. Just wondering if you could comment about the linearity of last quarter. It seems like there was a lot of concern early in the quarter and I know from the reports I've been hearing, things don't seem to be quite as bad as what people thought back in July.

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### Paul Zeller - Imation Corporation - VP and CFO

You know, let me take a first stab at that and then let Mark finish. But when you look at our particular quarterly progression and our kind of tie into macro conditions, I think there are a number of moving parts as we are transforming that our impacts that are more kind of our own are more relevant to our transformation than some of the macro factors you might see in the market.

I do think we saw weakness in retail that has continued and clearly that's driven by the macroeconomic environment. I think overall IT spending is reasonable but I don't think there was anything unique in terms of our monthly progression or comparisons to prior quarter.

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### Mark Lucas - Imation Corporation - President and CEO

I would agree with that, Mark. Retail is continuing to be soft. I think it's around the world. We are seeing that the forecast for the fourth quarter from independent analysts is somewhat mixed and uncertain. We are not sure how consumers are going to react to that.

On the business side of what we do in the OEM side, we continue to make pretty good progress. I think our strategic transformation into new product categories is very relevant to where business needs of our customers are going. And so we continue to be very optimistic about this transformation and the road we are taking.

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### Mark Miller - Noble Financial Markets - Analyst

Any exposure or opportunities seen? I hate to use that term because it is a tragic situation. But due to the flooding over in Thailand, I know it's dramatically impacted some of the disk drive companies and there are a lot of component suppliers over there in the various industries.



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**Mark Lucas** - *Imation Corporation - President and CEO*

Right now -- we source the majority of our HDD discs from Toshiba and we have gotten commitments from them for no interruption of supply chain because we actually don't get our drives out of Thailand. We get them out of some of their other factories. Obviously there could be some opportunity for us. But it's very, very uncertain right now.

**Mark Miller** - *Noble Financial Markets - Analyst*

Just wondering too, you've had a number of special effects that have hit cash. What does the cash outlook look like for this quarter?

**Paul Zeller** - *Imation Corporation - VP and CFO*

You mean looking forward, Mark?

**Mark Miller** - *Noble Financial Markets - Analyst*

Yes.

**Paul Zeller** - *Imation Corporation - VP and CFO*

Subject to any inorganic actions we take, I think the fundamental cash generative aspect of the business model continues. We have positive EBITDA. I think frankly we've got our inventories a little higher than they need to be and I think there's some opportunity to improve that over time. But -- and we have had to absorb this year some terms changes with our optical suppliers that have been a bit painful. That's really behind us at this stage.

So I really think that the same kind of cash generation reality we have seen should generally be the case subject to of course other unique cash investment opportunities.

**Mark Miller** - *Noble Financial Markets - Analyst*

Thank you.

**Operator**

Rich Rubin, Hawkeye Capital.

**Rich Rubin** - *Hawkeye Capital - Analyst*

Good morning. Clearly we are disappointed with the numbers. Our stock is down 10% today and we have seen the cash go from 305 at the end of 2010 to 233 at the end of September. We have seen tangible book go down. So I want to focus on the things that I think are really important here.

How have we spent the money on acquisitions? Can you talk us through the multiples and how you guys see those acquisitions working out? Then also on the restructuring savings and when we are going to see that hitting the numbers?



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**Paul Zeller** - *Imation Corporation - VP and CFO*

Let me start with kind of the cash investments over time. You have seen in the last 10-Q that we spent in the neighborhood of \$26 million on the MXI acquisition. We have not yet disclosed the acquisition price on IronKey and will as we move forward and finalize the transaction details. So you can assume some reasonable share of that \$70 million decline is due to the investments we made in acquisition.

In addition, there have been some impacts on working capital, as I mentioned just a minute ago, from the changes in some terms and losing the ability to have vendor consignment, one of those realities in the optical business. That was a function of the supplier cost issues they have been facing.

And so I think fundamentally the Company is and will continue to generate cash. We have made some investments, which gives to your second question about what are the multiples and the valuation dynamics of those investments?

We have talked in the past, Rich, about kind of two classes of investments, one which is going to be smaller, that's more about acquiring technology in a platform and an example of that would be the ENCRYPTX acquisition or the ProStor InfiniVault acquisition. The other side of the spectrum will be a larger acquisition where we are fundamentally buying a pretty existing revenue base and earnings potential. I would put the couple of acquisitions in the security space kind of in between the two.

We are buying into a rapidly growing market reality and security that we are very excited about. That is relatively in its infancy relative to the ultimate opportunity so there are real revenues, not profitability currently. But there's I think a great opportunity as we've built the number one position in the kind of removable security space. And we think that's a very strong platform for the future not just in that market category, but we think the technology is leverageable across a broader array of products as well.

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**Rich Rubin** - *Hawkeye Capital - Analyst*

Right. But you can't tell us the numbers on how you've spent our cash. So as shareholders you can use these terms like progress and they may sound great. We're not seeing anything. We are just seeing cash leave the balance sheet. We are seeing no insiders buying shares in the open market, so that shows us how confident you are.

And it just -- we have seen nothing to prove that this strategy is going to work. And yet your shares had been trading below cash and you don't aggressively buy back your shares. You know, it's a disappointment. And none of you guys buy back shares. None of you buy in the open market.

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**Mark Lucas** - *Imation Corporation - President and CEO*

Rich, this is Mark. You are very consistent in your comments to me. So I appreciate that. I totally understand what you are asking for. We have outlined very clearly I think what the strategic direction of this Company is, how we are going to best leverage our assets to increase shareholder return. We have said we are in a state of transition for 2011 and much of 2012. We plan to continue down that path. Now as we (multiple speakers)

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**Rich Rubin** - *Hawkeye Capital - Analyst*

You are following the path of Kodak. You are going to spend and (multiple speakers) and take a shot with shareholders' money and you have a ton of cash. The stock trades well below liquidation value. And you are doing nothing about it. You're just taking shots at acquisitions.

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**Mark Lucas** - *Imation Corporation - President and CEO*

Rich, again, I appreciate your comments. We have done some share buybacks and we will continue to evaluate that depending on stock price and market conditions. We are very committed to our strategy going forward. We're very thoughtful about what we do. We're very analytical about what we do and we believe we are making tremendous strides to return shareholder value over the long term.

This is not a short-term play for us. This is a long-term transformation that is going to eventually build tremendous value for shareholders. I understand your point of view. I think perhaps we just disagree with it.

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**Paul Zeller** - *Imation Corporation - VP and CFO*

Rich, if I could add one other specific comment to the Kodak discussion, I think it's very important to recognize what spaces we believe are prudent to invest in and those are spaces that are not highly competitive and with large capitalized companies already competing.

When we look at scalable storage, we are not really interested in going and getting involved in the enterprise level, competing against NetApp and IBM and the big guys. We like the SMB. That's got a lot more white space and smaller, frankly, competitors and greater opportunity.

Security, another example of a space where it's not dominated by large already present competitors. So I think there's a pretty significant difference between trying to think we are going to deploy cash against people that are already there in a significant way and I think that's kind of the platform building reality of what we are doing. And we are doing it with modest sized acquisitions, as we have described, and doing it very thoughtfully, in our opinion.

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**Rich Rubin** - *Hawkeye Capital - Analyst*

But you can't explain to us how you're -- the return on equity on those investments?

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**Paul Zeller** - *Imation Corporation - VP and CFO*

Well, we certainly are investing in opportunities (multiple speakers) that we believe will bring significant returns over the long term and every acquisition will vary depending on the growth opportunity, the margin profile, and frankly the risks associated with it.

So it's -- there's not one. The only common denominator here is it has to provide a substantial net present value and high internal rate of return or we are not going to pursue it.

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**Rich Rubin** - *Hawkeye Capital - Analyst*

Okay, guys.

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**Operator**

Chuck Murphy, Sidoti & Company.

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**Chuck Murphy** - *Sidoti & Co. - Analyst*

Good morning, guys. Did you mention kind of what was behind the sequential decline for secure and scalable? Was that a seasonality issue or --?

**Paul Zeller** - *Imation Corporation - VP and CFO*

Yes, there's a lot of differences quarter-to-quarter in terms of all of our product categories. If you look particularly at what's going on in secure and scalable storage, the sequential decline all about flash and you know flash is an opportunistic kind of place for our investment where when there's good margins, we will go after it and where there are not, we will scale back. And so that tends to -- we tend to go in and out in terms of some of those positions and if you were to adjust for the flash -- the sort of commodity flash category, we were up nicely sequentially.

**Chuck Murphy** - *Sidoti & Co. - Analyst*

I thought you had kind of gotten out of the commodity flash all together.

**Paul Zeller** - *Imation Corporation - VP and CFO*

No, it's still a meaningful part of that secure and scalable storage strategy today. We got out kind of the retail and highly price-sensitive categories. We are involved for the most part in commercial channels or in certain international channels and not for example in US retail.

**Chuck Murphy** - *Sidoti & Co. - Analyst*

Got you, and my other set of questions had to do with the optical business and what you were talking about with the price pressures. Can you kind of give us some more color on that \$7.2 million levy benefit? And then also you mentioned something. I didn't catch whether you said you had already done price increases or you were looking to do price increases.

**Mark Lucas** - *Imation Corporation - President and CEO*

Yes, Chuck, this is Mark. On the price increase side, we are implementing them across the board internationally in different phased approaches. Obviously with our key customers, it is a bit of a negotiation and it is very difficult in this economic climate to get through some of the increases that we have, but we are being successful for the most part.

The cost increases have gone up about 45% this year, so really, really significant for us. We have managed that I think extremely well and long-term we believe there will be some stability return to this marketplace and we will continue to do well.

I will let Paul talk specifically about the levy situation.

**Paul Zeller** - *Imation Corporation - VP and CFO*

The whole levy reality is nothing if not complex and let me kind of give you the Cliff's Notes version. It's a big number obviously and we've had some other impacts in the year.

It has to do with the way in which Europe compensates kind of artists for copywritten material and the way it works is the importer of record for optical discs, that being us in most countries in Europe, we are required to pay a royalty to collecting



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societies in every country and then they remit that to the artists. There are EC level rules that specify that. The basis for doing that is for the legal copying of content for consumers.

There has been an ongoing dispute in the industry about whether that rule should apply to optical discs being sold into commercial channels and based on our background and our heritage going all the way back to diskettes at 3M, we have a pretty good commercial channel presence in Europe.

Last year the ECJ, the European Court of Justice, ruled in favor of those of us that made that claim about commercial levies and we stopped paying commercial levies last year, though we continue to accrue them while we awaited kind of what local courts would do in applying that Central European rule. And we have started seeing local jurisdictions kind of deal with the issue in a positive manner and we have started reversing some of the accruals related to those countries. That's why we had a couple million dollar benefit in first quarter, about \$3.4 million in second quarter and now \$7.2 million this quarter.

We do think there is a potential for continuing benefits looking forward, though there's no certainty with that. So we are going to continue to provide the details if and when we get benefits in levies quarter by quarter.

The benefits we have been getting along with price increase actions have allowed us to offset the impact from this industrywide kind of cost increases we've had to absorb. And in the quarter if you kind of net all the factors of the levy benefit, the benefit from price increases we've taken into the channel, and the penalty from cost increases, there was a modest benefit, maybe \$1.5 million of a benefit on our results. In prior quarters, it's actually kind of netted to a penalty. So that's kind of the long and short of it on levies.

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**Chuck Murphy** - *Sidoti & Co. - Analyst*

Okay, and where did that hit in the quarter? Was that SG&A or --?

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**Paul Zeller** - *Imation Corporation - VP and CFO*

Gross margin.

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**Chuck Murphy** - *Sidoti & Co. - Analyst*

Gross, okay. That's all I had. Thanks, guys.

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**Operator**

(Operator Instructions). There are no further questions at this time.

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**Mark Lucas** - *Imation Corporation - President and CEO*

Great. Well, thank you, everyone, for your interest and we look forward to talking to you again next quarter. Goodbye.

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**Operator**

Ladies and gentlemen, this concludes today's conference call. Thank you for your participation. You may now disconnect. Good day.

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