SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

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# FORM 10-Q

(Mark One)

[ X ] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 1995

[ ] 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
0-16439

FAIR, ISAAC AND COMPANY, INCORPORATED
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| DELAWARE | 94-1499887 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

120 North Redwood Drive, San Rafael, California 94903
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (415) 472-2211

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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 x No .

The number of shares of Common Stock, $0.01 par value per share, outstanding on February 9, 1996, was 12,401,510.

TABLE OF CONTENTS

PART I - FINANCIAL INFORMATION

ITEM 1. Financial Statements.

FAIR, ISAAC AND COMPANY, INCORPORATED

CONSOLIDATED BALANCE SHEETS

December 31, 1995 and September 30, 1995

(dollars in thousands)

| | December 31 (unaudited) | September 30 (audited) |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 11,929 | $ 8,321 |
| Short-term investments | 4,496 | 5,874 |
| Accounts receivable, net | 18,112 | 19,094 |
| Unbilled work in progress | 7,892 | 11,299 |
| Deferred income taxes | 1,397 | 1,399 |
| Prepaid expenses and other current assets | 2,351 | 1,784 |
| Total current assets | 46,177 | 47,771 |
| Noncurrent assets: | | |
| Long-term investments | 11,351 | 10,923 |
| Note receivable | 2,890 | 2,895 |
| Property and equipment, net | 18,222 | 16,815 |
| Intangibles, net | 4,488 | 4,957 |
| Deferred income taxes and other assets | 4,550 | 4,929 |
| | $ 87,678 | $ 88,290 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable and other accrued liabilities | $ 6,697 | $ 5,830 |
| Accrued compensation and employee benefits | 6,054 | 10,631 |
| Billings in excess of earned revenues | 5,500 | 5,314 |
| Income taxes payable | 2,065 | 1,603 |
| Total current liabilities | 20,316 | 23,378 |
| Deferred income taxes and other liabilities | 4,948 | 6,854 |
| Capital leases | 1,799 | 1,930 |
| Commitments and contingencies | -- | -- |
| Total liabilities | 27,063 | 32,162 |
| Stockholders' equity: | | |
| Common stock | 125 | 123 |
| Paid-in capital in excess of par value | 15,568 | 14,508 |
| Retained earnings | 45,163 | 41,975 |
| Less treasury stock (18,161 shares at cost at 12/31/95; 53,562 at 9/30/95) | (56) | (228) |
| Less pension adjustment | (406) | (406) |
| Unrealized gain on investment | 221 | 156 |
| Total stockholders' equity | 60,615 | 56,128 |
| | $ 87,678 | $ 88,290 |

See accompanying notes to the consolidated financial statements.

FAIR, ISAAC AND COMPANY, INCORPORATED

CONSOLIDATED STATEMENTS OF INCOME

For the three months ended December 31, 1995 and 1994
(in thousands except per share data)

| | Three Months Ended December 31 (Unaudited) 1995 | 1994 |
|---|---|---|
| Revenues | $ 32,628 | $ 25,632 |
| Costs and expenses: | | |
| Cost of revenues | 13,173 | 9,337 |
| Sales and marketing | 5,396 | 5,350 |
| Research and development | 760 | 1,213 |
| General and administrative | 7,355 | 5,042 |
| Amortization of intangibles | 288 | 330 |
| Total costs and expenses | 26,972 | 21,272 |
| Income from operations | 5,656 | 4,360 |
| Interest and other income (net) | 317 | 373 |
| Income before income taxes | 5,973 | 4,733 |
| Income tax provision | 2,449 | 1,911 |
| Net income | $ 3,524 | $ 2,822 |
| Earnings per share | $ .28 | $ .22 |
| Shares used in computing earnings per share | 12,761,000 | 12,676,000 |

See accompanying notes to the consolidated financial statements.

FAIR, ISAAC AND COMPANY, INCORPORATED

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the three months ended December 31, 1995 and 1994
(dollars in thousands)

(UNAUDITED)

| | 1995 | 1994 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $ 3,524 | $ 2,822 |
| Adjustments to reconcile net income to cash provided by operating activities: | | |
| Depreciation and amortization | 1,995 | 1,387 |
| Decrease in accounts receivable and unbilled work in progress | 4,394 | 2,195 |
| (Increase)/Decrease in prepaid expenses and other | 183 | (293) |
| Decrease in accrued compensation and employee benefits | (5,504) | (4,384) |
| Increase in accounts payable and other liabilities | 500 | 461 |
| (Increase)/Decrease in income taxes payable | 462 | (106) |
| Increase in billings in excess of contract costs | 186 | 30 |
| Net cash provided by operating activities | 5,740 | 2,112 |
| Cash flows from investing activities: | | |
| Purchases of property, equipment and computer software | (3,068) | (1,866) |
| Purchases of investments | (806) | (3,202) |
| Proceeds from maturities of investments | 1,862 | 2,000 |
| Net cash used by investing activities | (2,012) | (3,068) |
| Cash flows from financing activities: | | |
| Reduction of capital lease obligations | (131) | (82) |
| Issuance of common stock | 255 | 312 |
| Dividends paid | (244) | -- |
| Net cash used by financing activities | (120) | 230 |
| Increase/(Decrease) in cash and cash equivalents | 3,608 | (726) |
| Cash and cash equivalents, beginning of period | 8,321 | 10,990 |
| Cash and cash equivalents, end of period | $11,929 | $10,264 |

See accompanying notes to the consolidated financial statements.

FAIR, ISAAC AND COMPANY, INCORPORATED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Income taxes paid

Cash payments for income taxes during the three-month periods ended December 31, 1995, and 1994 were $1,964,000 and $1,556,000 respectively.

Note 2 Non-cash transactions

The Company contributed treasury stock having a market value of $979,000 and $848,000 to the Company's Employee Stock Ownership Plan during the first fiscal quarters of 1996 and 1995, respectively.

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

### General

Fair, Isaac and Company, Incorporated, provides products and services designed to help a variety of businesses use data to make better decisions on their customers and prospective customers. The Company's products include statistically derived, rule-based analytical tools, software designed to implement those analytical tools, and consulting services to help clients use and track the performance of those tools. The Company also provides a range of credit scoring and credit account management services in conjunction with credit bureaus and credit card processing agencies. Its DynaMark subsidiary provides data processing, database management and personalized printing services to businesses engaged in direct marketing.

The Company is organized into business units which correspond to its principal markets: consumer credit, insurance and direct marketing (DynaMark). Sales to the consumer credit industry have traditionally accounted for the bulk of the Company's revenues. Products developed specifically for a single user in this market are generally sold on a fixed-price basis. Such products include application and behavior scoring algorithms (also known as "analytic products" or "scorecards"), credit application processing systems (ASAP and CreditDesk) and custom credit account management systems including those marketed under the name TRIAD. Software systems usually also have a component of ongoing maintenance revenue, and CreditDesk systems have also been sold under time- or volume-based price arrangements. Credit scoring and credit account management services sold through credit bureaus and third-party credit card processors are generally priced based on usage. Products sold to the insurance industry are generally priced based on the number of policies in force, subject to contract minimums. DynaMark employs a combination of fixed-fee and usage-based pricing.

### Results of Operations
### Revenues

The following table sets forth for the fiscal periods indicated (a) the percentage of revenues contributed by the DynaMark and Insurance business units, and the percentage of revenues represented by fixed-price and usage-priced revenues from the Credit business unit; and (b) the percentage change in revenues within each category from the corresponding period in the prior fiscal year. Fixed-price revenues include all revenues from application processing software, custom scorecard development and consulting projects for credit. Virtually all usage revenues are generated through third-party alliances such as those with credit bureaus and third-party credit card processors.

| | Percentage of Revenue Quarter Ended December 31, | | Period-to-Period Percentage Changes Quarter Ended 12/31/95 compared to 12/31/94 |
|---|---|---|---|
| | 1995 | 1994 | |
| Credit: | | | |
| Fixed-price | 27% | 26% | 31% |
| Usage-priced | 55 | 55 | 28 |
| DynaMark | 15 | 17 | 10 |
| Insurance | 3 | 2 | 79 |
| Total revenues | 100% | 100% | 27 |

The increase in usage revenues in the quarter ended December 31, 1995, compared with the same period the prior year, was due to continuing growth in usage of the Company's scoring services distributed through the three major credit bureaus in the United States, including the PreScore(R) and ScoreNet(R) services, and growth in the number of credit accounts managed under the services delivered through third-party processors. Revenues from sales of credit application scoring systems, credit application processing software, and credit account management systems were all up significantly in the quarter ended December 31, 1995, compared with the quarter ended December 31, 1994, accounting for the growth in fixed-price credit revenues. Insurance revenues increased by 79 percent due to growth in the acceptance of both end-user custom products and the insurance scoring services distributed through consumer reporting agencies. DynaMark's revenue growth was well below the Company average, primarily because of the loss of one large project to a competitor.

Revenues from credit bureau-related services have increased rapidly in each of the last three fiscal years and accounted for approximately 39 percent of revenues in fiscal 1995. Revenues from services provided through bankcard processors also increased in each of these years, due primarily to increases in the number of accounts at each of the major processors. While the Company has been very successful in extending or renewing its agreements with credit bureaus and bankcard processors in the past, and believes it will generally be able to do so in the future, the loss of one or more such alliances could have a significant impact on revenues and operating margin. Revenues generated through the Company's alliances with Equifax, Inc., TRW, Inc. and Trans Union Corporation each accounted for approximately nine to eleven percent of the Company's total revenues in fiscal 1995.

Potential new government regulation of the use of credit bureau data could have an impact on the use of any of the Company's credit bureau scoring services including PreScore(R) and ScoreNet(R). Bills which would substantially amend the Fair Credit Reporting Act were introduced in each of the last three Congresses and at least two such bills were introduced in 1995. These bills would impose new restrictions on the use of credit bureau data to prescreen solicitation lists. Bills and regulations have also been introduced, and, in some cases enacted, at the state level that affect the use of credit bureau data in various ways, including restricting the use of such data in making insurance underwriting decisions. State regulation of credit bureau data, particularly regulations imposing requirements on the credit bureaus or users of credit bureau information which differ from those existing under federal law, may also have an adverse impact on bureau scoring services. The Company believes certain enacted or pending state legislation and regulation of credit bureau data in connection with insurance underwriting has had a negative impact on its efforts to sell insurance risk scores through credit reporting agencies. However, the Company cannot predict whether any other particular federal or state legislation affecting credit bureau information or credit scoring is likely to be enacted in the foreseeable future, or the extent to which the passage of such legislation might affect the Company's business.

Revenues derived from outside of the United States represented approximately 14 percent of total revenues in the quarter ended December 31, 1995, compared with 11 percent of total revenues in the same period a year earlier.

During the period from 1990 through 1994, while the rate of account growth in the U.S. bankcard industry was slowing and many of the Company's largest institutional clients were merging and consolidating, the Company generated above-average growth in revenues--even after correcting for the effect of the DynaMark acquisition--from its bankcard-related scoring and account management business by deepening its penetration of large banks and other credit issuers. The Company's revenues grew by 26 percent in fiscal 1995 which is closer to what the Company believes is a sustainable, long-term growth rate than the growth rates in 1990 through 1994. The Company believes much of its future growth prospects will depend on several important factors, including those discussed above and its ability (1) to develop new, high value products and services for its present client base of major U.S. consumer credit issuers; (2) to increase its penetration of established or emerging credit markets outside the U.S. and Canada; and (3) to expand--either directly or through further acquisitions--into relatively undeveloped or underdeveloped markets for its products and services such as direct marketing, insurance, small business lending, and health care information management.

Over the long term, in addition to the factors discussed above, the Company's rate of revenue growth--excluding growth due to acquisitions--is limited by the rate at which it can recruit and absorb additional professional staff. While the increasing percentage of usage revenues may loosen this constraint to some extent, management believes it will continue to exist indefinitely. On the other hand, despite the high penetration the Company has already achieved in certain markets, the opportunities for application of its core competencies are much greater than it can pursue. Thus, the Company believes it can continue to grow revenues, within the personnel constraint, for the foreseeable future. At times management may forego short-term revenue growth in order to devote limited resources to opportunities which it believes have exceptional long-term potential. This occurred in the period from 1988 through 1990 when the Company devoted significant resources to developing the usage priced services distributed through credit bureaus and third-party processors. Cumulative revenue since 1987, net of the DynaMark acquisition, is very close to the Company's twenty-year historical average revenue growth of 21 percent.

Expenses

The following table sets forth for the periods indicated (a) the percentage of revenues represented by certain line items in the Company's consolidated statement of income and (b) the percentage change in such items from the same quarter in the prior fiscal year.

| | Percentage of Revenue | | Period-to-Period Percentage Changes |
|---|---|---|---|
| | Quarter Ended December 31, | | Quarter Ended 12/31/95 Compared to Quarter Ended 12/31/94 |
| | 1995 | 1994 | |
| Revenues ........................... | 100% | 100% | 27% |
| Costs and expenses: | | | |
| Cost of revenues ............... | 40 | 36 | 41 |
| Sales and marketing ............ | 17 | 21 | 1 |
| Research and development ....... | 2 | 5 | (37) |
| General and administrative ..... | 23 | 20 | 46 |
| Amortization of intangibles..... | 1 | 1 | (13) |
| Total costs and expenses ....... | 83 | 83 | 27 |
| Income from operations ............ | 17 | 17 | 30 |
| Interest and other income, net..... | 1 | 1 | (15) |
| Income before income taxes ........ | 18 | 18 | 26 |
| Income tax provision .............. | 7 | 7 | 28 |
| Net income ........................ | 11% | 11% | 25% |

Costs of Revenues

Cost of revenues consists primarily of personnel, travel, and related overhead costs; costs of computer service bureaus; the amounts paid by the Company to credit bureaus for scores and related information in connection with the ScoreNet Service, and depreciation. The cost of revenues, as a percentage of net revenues, increased in the quarter ended December 31, 1995, as compared with the same quarter a year earlier, primarily because DynaMark's revenues were below planned levels while corresponding expenses could not be reduced on a short-term basis.

Sales and Marketing

Sales and marketing expenses consist principally of personnel, travel, overhead, advertising and other promotional expenses. These expenses, as a percentage of revenues, decreased primarily due to reductions in advertising expenses.

Research and Development

Research and development expenses include the personnel and related overhead costs incurred in product development, researching mathematical and statistical algorithms, and developing software tools that are aimed at improving productivity and management control. Research and development expenses, as a percentage of revenues, decreased from the same period of fiscal 1995 because of lower research and development efforts with respect to credit bureau products.

General and Administrative

General and administrative expenses consist mainly of compensation expenses for certain senior management, corporate facilities expenses, the costs of administering benefit plans, legal expenses, and the costs of operating administrative functions such as finance and computer information systems. As a percentage of revenues these expenses increased significantly compared with the same quarter of fiscal 1995 primarily due to increases in office space, expenditures made to improve the Company's information systems and technology infrastructure, and the research associated with exploring new business opportunities, particularly in the area of health care information management. Significant increases in the levels of such expenses occurred during the later part of fiscal 1995. General and administrative expenses for the quarter ended December 31, 1995, were five percent higher than in the immediately preceding quarter.

Financial Condition

Working capital increased from $24,393,000 at September 30, 1995 to $25,861,000 at December 31, 1995; and cash and investments increased from $25,118,000 at September 30, 1995, to $27,776,000 at December 31, 1995. The Company has no long-term debt other than capital lease and employee incentive obligations. The Company believes that cash and marketable securities on hand are adequate to meet its capital and liquidity needs for the foreseeable future.

Interim Periods

The Company believes that all the necessary adjustments have been included in the amounts shown in the consolidated financial statements contained in Item 1 above for the three-month periods ended December 31, 1995 and 1994 to state fairly the results for such interim periods. This includes all normal recurring adjustments that the Company considers necessary for a fair statement thereof, in accordance with generally accepted accounting principles. This report should be read in conjunction with the Company's 1995 Form 10-K.

Quarterly results may be affected by fluctuations in revenues associated with credit card solicitations, by the timing of orders for and deliveries of certain ASAP and TRIAD systems, and by the seasonality of ScoreNet purchases. With the exception of the cost of ScoreNet data purchased by the Company, most of its operating expenses are not affected by short-term fluctuations in revenue, and thus such revenue fluctuations may have a significant impact on operating results. However, in recent years, these fluctuations were generally offset by the strong growth in revenues from services delivered through credit bureaus and third-party bankcard processors.

Management believes that neither the quarterly variation in revenues and net income, nor the results of operations for any particular quarter, are necessarily indicative of results of operations for full fiscal years. Accordingly, management believes that the Company's results should be evaluated on an annual basis.

## PART II - OTHER INFORMATION

ITEM 4. Submission of Matters to a Vote of Security Holders.

At the Annual Meeting of Stockholders of the Company held on February 6, 1996, the Company's stockholders voted in favor of: (i) the election of eight directors to the Company's Board of Directors, (ii) an amendment of the Company's Restated Certificate of Incorporation increasing the number of authorized shares of Common Stock from 15,000,000 to 35,000,000 shares; (iii) amendments to the Company's 1992 Long-term Incentive Plan; and (iv) the ratification of KPMG Peat Marwick LLP as the Company's independent auditors. The number of votes for, withheld and against, as well as the number of abstentions and broker non-votes as to each matter approved at the Annual Meeting of Stockholders were as follows:

| Matter | For | Withheld | Against | Abstain | Broker Non-votes |
|---|---|---|---|---|---|
| Election of Directors | | | | | |
| Bryant J. Brooks, Jr. | 11,017,187 | 125,305 | N/A | N/A | 0 |
| H. Robert Heller | 11,017,008 | 125,484 | N/A | N/A | 0 |
| Guy R. Henshaw | 11,016,006 | 126,486 | N/A | N/A | 0 |
| David S.P. Hopkins | 11,017,987 | 124,505 | N/A | N/A | 0 |
| Robert M. Oliver | 11,017,787 | 124,705 | N/A | N/A | 0 |
| Larry E. Rosenberger | 11,018,787 | 123,705 | N/A | N/A | 0 |
| Robert D. Sanderson | 10,925,564 | 216,928 | N/A | N/A | 0 |
| John D. Woldrich | 11,018,787 | 123,705 | N/A | N/A | 0 |
| Increase in Authorized Shares of Common Stock | 9,054,262 | N/A | 2,046,888 | 41,342 | 0 |
| Amendments to 1992 Long-term Incentive Plan | 8,902,611 | N/A | 967,261 | 19,904 | 1,252,716 |
| Ratification of Auditors | 11,121,453 | N/A | 13,390 | 7,649 | 0 |

ITEM 6. Exhibits and Reports on Form 8-K.

(a) Exhibits:

11.1 Computation of Earnings per Share.

24.1 Power of Attorney (see page 12 of this Form 10-Q).

27 Financial Data Schedule.

(b) Reports on Form 8-K:

None.

## SIGNATURES

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

FAIR, ISAAC AND COMPANY, INCORPORATED

DATE: February 12, 1996

By GERALD DE KERCHOVE
------------------------------------
Gerald de Kerchove
Executive Vice President

## POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that the person whose signature appears below constitutes and appoints PETER L. McCORKELL his attorney-in-fact, with full power of substitution, for him in any and all capacities, to sign any amendments to this Report on Form 10-Q and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that said attorney-in-fact, or his substitute or substitutes, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following person on behalf of the registrant and in the capacities and on the date indicated.

DATE: February 12, 1996

By PATRICIA COLE
------------------------------------
Patricia Cole
Controller
(Chief Accounting Officer)

EXHIBIT INDEX
TO FAIR, ISAAC AND COMPANY, INCORPORATED
REPORT ON FORM 10-Q FOR THE QUARTER ENDED DECEMBER 31, 1995

Exhibit 11.1

FAIR, ISAAC AND COMPANY, INCORPORATED
COMPUTATION OF EARNINGS PER SHARE
(IN THOUSANDS EXCEPT PER SHARE DATA)

| | Three months ended December 31, 1995 | 1994 |
| --- | --- | --- |
| Primary Earnings Per Share: | | |
| Weighted Average Common Shares Outstanding | 12,282 | 12,124 |
| Shares Issuable Upon Exercise of Stock Options | 759 | 760 |
| Less Shares Assumed to be Repurchased | (280) | (208) |
| Weighted Average Common Shares, as Adjusted | 12,761 | 12,676 |
| Net Income | $ 3,524 | $ 2,882 |
| Primary Earnings per Share | $ 0.28 | $ 0.22 |
| Fully Diluted Earnings Per Share: | | |
| Weighted Average Common Shares Outstanding | 12,282 | 12,124 |
| Shares Issuable Upon Exercise of Stock Options | 755 | 760 |
| Less Shares Assumed to be Repurchased | (303) | (156) |
| Weighted Average Common Shares, as Adjusted | 12,734 | 12,728 |
| Net Income | $ 3,524 | $ 2,882 |
| Fully Diluted Earnings Per Share | $ 0.28 | $ 0.22 |

5

This schedule contains Summary Financial Information extracted from the Consolidated Balance Sheets and Income Statements and is qualified in its entirety by reference to such financial statements.

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3-MOS

SEP-30-1995
DEC-31-1995
11,929
4,496
18,442
330
0
46,177
31,851
13,629
87,678
20,316
0
125
0
0
60,490
87,678
32,628
32,628
0
26,972
0
0
46
5,973
2,449
3,524
0
0
0
3,524
.28
.28