

REALNETWORKS INC
Form 10-Q
November 06, 2014

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 September 30, 2014

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 0-23137

RealNetworks, Inc.

(Exact name of registrant as specified in its charter)

Washington

91-1628146

(State of incorporation)

(I.R.S. Employer

Identification Number)

1501 First Avenue South, Suite 600

98134

Seattle, Washington

(Address of principal executive offices)

(Zip Code)

(206) 674-2700

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐

Accelerated filer

☒

Non-accelerated filer ☐ (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 ☒

The number of shares of the registrant's Common Stock outstanding as of October 31, 2014 was 36,034,025.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

REALNETWORKS, INC. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	September 30, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	\$114,073	\$151,235
Short-term investments	63,948	74,920
Trade accounts receivable, net of allowances	17,679	24,613
Deferred costs, current portion	1,023	1,601
Deferred tax assets, net, current portion	296	306
Prepaid expenses and other current assets	8,382	9,124
Total current assets	205,401	261,799
Equipment, software, and leasehold improvements, at cost:		
Equipment and software	83,230	86,721
Leasehold improvements	3,616	3,482
Total equipment, software, and leasehold improvements, at cost	86,846	90,203
Less accumulated depreciation and amortization	68,392	67,031
Net equipment, software, and leasehold improvements	18,454	23,172
Restricted cash equivalents and investments	3,000	3,000
Equity method investment	10,000	12,473
Available for sale securities	2,848	7,181
Other assets	2,925	2,332
Deferred costs, non-current portion	913	946
Deferred tax assets, net, non-current portion	1,424	1,409
Other intangible assets, net	10,954	12,993
Goodwill	17,615	17,476
Total assets	\$273,534	\$342,781
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$18,155	\$19,987
Accrued and other current liabilities	25,885	41,893
Deferred tax liabilities, net, current portion	768	899
Deferred revenue, current portion	6,908	7,498
Total current liabilities	51,716	70,277
Deferred revenue, non-current portion	143	166
Deferred rent	1,293	1,318
Deferred tax liabilities, net, non-current portion	1,805	1,556
Other long-term liabilities	563	483
Total liabilities	55,520	73,800
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, \$0.001 par value, no shares issued and outstanding:		
Series A: authorized 200 shares	—	—
Undesignated series: authorized 59,800 shares	—	—
	36	36

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Common stock, \$0.001 par value authorized 250,000 shares; issued and outstanding 36,034 shares in 2014 and 35,833 shares in 2013

Additional paid-in capital	616,260	610,167	
Accumulated other comprehensive loss	(53,778	) (47,695)
Retained deficit	(344,504	) (293,527)
Total shareholders' equity	218,014	268,981	
Total liabilities and shareholders' equity	\$273,534	\$342,781	

See accompanying notes to unaudited condensed consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES
 UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 AND COMPREHENSIVE INCOME (LOSS)
 (In thousands, except per share data)

	Quarters Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net revenue (A)	\$34,157	\$48,958	\$120,706	\$155,601
Cost of revenue (B)	18,928	18,990	58,500	59,015
Extinguishment of liability (See Note 10)	—	—	(10,580)	—
Gross profit	15,229	29,968	72,786	96,586
Operating expenses:				
Research and development	12,784	15,707	40,110	45,951
Sales and marketing	13,283	19,427	51,022	59,830
General and administrative	7,723	9,869	25,617	28,506
Restructuring and other charges	2,048	1,877	3,805	4,075
Lease exit and related charges	154	—	703	3,066
Loss on legal settlements	—	11,525	—	11,525
Total operating expenses	35,992	58,405	121,257	152,953
Operating income (loss)	(20,763)	(28,437)	(48,471)	(56,367)
Other income (expenses):				
Interest income, net	80	166	396	992
Gain (loss) on sale of available for sale securities, net	—	—	2,371	—
Equity in net loss of Rhapsody investment	(1,530)	(2,629)	(4,170)	(6,209)
Other income (expense), net	325	(118)	153	(146)
Total other income (expenses), net	(1,125)	(2,581)	(1,250)	(5,363)
Income (loss) before income taxes	(21,888)	(31,018)	(49,721)	(61,730)
Income tax expense (benefit)	290	357	1,256	(210)
Net income (loss)	\$(22,178)	\$(31,375)	\$(50,977)	\$(61,520)
Basic net income (loss) per share	\$(0.62)	\$(0.88)	\$(1.42)	\$(1.73)
Diluted net income (loss) per share	\$(0.62)	\$(0.88)	\$(1.42)	\$(1.73)
Shares used to compute basic net income (loss) per share	36,003	35,670	35,912	35,490
Shares used to compute diluted net income (loss) per share	36,003	35,670	35,912	35,490
Comprehensive income (loss):				
Unrealized investment holding gains (losses), net of reclassification adjustments	\$(323)	\$(1,043)	\$(3,936)	\$(28)
Foreign currency translation adjustments, net of reclassification adjustments	(2,338)	1,235	(2,147)	(391)
Total other comprehensive income (loss)	(2,661)	192	(6,083)	(419)
Net income (loss)	(22,178)	(31,375)	(50,977)	(61,520)
Comprehensive income (loss)	\$(24,839)	\$(31,183)	\$(57,060)	\$(61,939)
(A) Components of net revenue:				
License fees	\$5,925	\$10,503	\$21,168	\$33,494
Service revenue	28,232	38,455	99,538	122,107
	\$34,157	\$48,958	\$120,706	\$155,601
(B) Components of cost of revenue:				
License fees	\$2,044	\$2,062	\$6,426	\$6,377
Service revenue	16,884	16,928	52,074	52,638
	\$18,928	\$18,990	\$58,500	\$59,015

See accompanying notes to unaudited condensed consolidated financial statements.

REALNETWORKS, INC. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Nine Months Ended September 30,	
	2014	2013
Cash flows from operating activities:		
Net income (loss)	\$(50,977	) \$(61,520
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	8,876	15,045
Stock-based compensation	4,158	5,671
Equity in net loss of Rhapsody	4,170	6,209
Deferred income taxes, net	(64	) (1,238
Gain on sale of available for sale securities	(2,371) —
Realized translation gain	(48	) (35
Extinguishment of liability	(10,580) —
Other	—	51
Net change in certain operating assets and liabilities:		
Trade accounts receivable	6,553	6,466
Prepaid expenses and other assets	1,353	4,772
Accounts payable	(1,606	) 26
Accrued and other liabilities	(5,106	) (3,750
Net cash provided by (used in) operating activities	(45,642	) (28,303
Cash flows from investing activities:		
Purchases of equipment, software, and leasehold improvements	(2,054	) (5,798
Proceeds from sale of available for sale securities	2,754	—
Purchases of short-term investments	(63,574	) (85,670
Proceeds from sales and maturities of short-term investments	74,546	110,359
Decrease (increase) in restricted cash equivalents and investments, net	—	5,000
Acquisitions of businesses, net of cash acquired	(733	) (22,480
Other	(467) —
Net cash provided by (used in) investing activities	10,472	1,411
Cash flows from financing activities:		
Proceeds from issuance of common stock (stock options and stock purchase plan)	641	408
Tax payments from shares withheld upon vesting of restricted stock	(403	) (911
Payment of contingent consideration	(696	) (828
Net cash provided by (used in) financing activities	(458)