

ROSETTA STONE INC
Form 10-Q
November 13, 2009

Use these links to rapidly review the document

[ROSETTA STONE INC. Table of Contents](#)

[Table of Contents](#)

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2009

Commission File Number: 1-34283

ROSETTA STONE INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation or organization)

**1919 North Lynn St., 7th Fl,
Arlington, Virginia**
(Address of Principal Executive Offices)

043837082
(I.R.S Employer
Identification No.)

22209
(Zip Code)

800-788-0822

(Registrant's telephone number, including zip 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 Website, 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.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a 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

Edgar Filing: ROSETTA STONE INC - Form 10-Q

Indicate the number of shares outstanding of each of the issuer's classes of stock, as of the latest practicable date.

As of November 9, 2009, 20,363,616 shares of the registrant's Common Stock, \$.00005 par value, were outstanding.

Table of Contents

ROSETTA STONE INC.

Table of Contents

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1</u> <u>Financial Statements</u>	<u>3</u>
<u>Item 2</u> <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>23</u>
<u>Item 3</u> <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>39</u>
<u>Item 4T</u> <u>Controls and Procedures</u>	<u>39</u>
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1</u> <u>Legal Proceedings</u>	<u>40</u>
<u>Item 1A</u> <u>Risk Factors</u>	<u>40</u>
<u>Item 2</u> <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>59</u>
<u>Item 3</u> <u>Defaults Upon Senior Securities</u>	<u>60</u>
<u>Item 4</u> <u>Submission of Matters to a Vote of Security Holders</u>	<u>60</u>
<u>Item 5</u> <u>Other Information</u>	<u>60</u>
<u>Item 6</u> <u>Exhibits</u>	<u>61</u>
<u>Signatures</u>	<u>62</u>

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****ROSETTA STONE INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(in thousands, except per share amounts)**

	September 30, 2009	December 31, 2008
	(unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 71,168	\$ 30,626
Restricted cash	64	34
Accounts receivable (net of allowance for doubtful accounts of \$1,643 and \$1,103, respectively)	40,470	26,497
Inventory, net	8,726	4,912
Prepaid expenses and other current assets	7,160	6,598
Income tax receivable	4,470	
Deferred income taxes	2,282	2,282
Total current assets	134,340	70,949
Property and equipment, net	18,625	15,727
Goodwill	34,199	34,199
Intangible assets, net	10,610	10,645
Deferred income taxes	6,828	6,828
Other assets	790	470
Total assets	\$ 205,392	\$ 138,818
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 3,456	\$ 3,207
Accrued compensation	7,615	8,570
Other current liabilities	23,832	21,353
Deferred revenue	25,433	14,382
Current maturities of long-term debt related party (Note 8)		4,250
Total current liabilities	60,336	51,762
Long-term debt related parties (Note 8)		5,660
Deferred revenue	1,728	1,362
Other long-term liabilities	623	963
Total liabilities	62,687	59,747
Commitments and contingencies (Note 12)		
Stockholders' equity:		
Class A, Series A-1 Convertible Preferred Stock, \$0.001 par value; zero and 269 shares authorized; zero and 269 shares issued and outstanding at September 30, 2009 and December 31,		26,876

Edgar Filing: ROSETTA STONE INC - Form 10-Q

2008, respectively		
Class A, Series A-2 Convertible Preferred Stock, \$0.001 par value; zero and 178 shares authorized; zero and 178 shares issued and outstanding at September 30, 2009 and December 31, 2008, respectively		17,820
Class B Convertible Preferred Stock, \$0.001 par value; zero and 115 shares authorized; zero and 111 issued and outstanding at September 30, 2009 and December 31, 2008, respectively		11,341
Preferred Stock, \$0.001 par value; 10,000 and zero shares authorized; zero and zero shares issued and outstanding at September 30, 2009 and December 31, 2008, respectively		
Class A Convertible Common Stock, \$0.00005 par value; zero and 900 shares authorized; zero and zero shares issued and outstanding at September 30, 2009 and December 31, 2008, respectively		
Class B Convertible Common Stock, \$0.00005 par value; zero and 20,000 shares authorized; zero and zero shares issued and outstanding at September 30, 2009 and December 31, 2008, respectively		
Non-designated common stock, \$0.00005 par value, 190,000 and 39,100 shares authorized; 20,364 and 1,936 shares issued and outstanding at September 30, 2009 and December 31, 2008, respectively	2	1
Additional paid-in capital	129,258	10,814
Accumulated income	13,629	12,422
Accumulated other comprehensive loss	(184)	(203)
Total stockholders' equity	142,705	79,071
Total liabilities and stockholders' equity	\$ 205,392	\$ 138,818

See accompanying notes to condensed consolidated financial statements.

Table of Contents

ROSETTA STONE INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(unaudited)		(unaudited)	
Revenue:				
Product	\$ 58,151	\$ 53,139	\$ 149,663	\$ 124,988
Subscription and service	9,065	6,664	24,297	18,143
Total revenue	67,216	59,803	173,960	143,131
Cost of revenue:				
Cost of product revenue	7,798	7,871	20,934	17,869
Cost of subscription and service revenue	1,210	705	2,204	1,789
Total cost of revenue	9,008	8,576	23,138	19,658
Gross profit	58,208	51,227	150,822	123,473
Operating expenses				
Sales and marketing	32,263	25,727	83,023	65,510
Research and development	6,125	5,018	21,069	13,308
General and administrative	11,914	8,889	44,967	26,272
Total operating expenses	50,302	39,634	149,059	105,090
Income from operations	7,906	11,593	1,763	18,383
Other income and (expense):				
Interest income	55	109	109	423
Interest expense	(8)	(194)	(348)	(714)
Other income (expense)	45	(31)	81	81
Total other income (expense)	92	(116)	(158)	(210)
Income before income taxes	7,998	11,477	1,605	18,173
Income tax provision	2,695	5,456	399	9,222
Net income	5,303	6,021	1,206	8,951
Earnings per share:				
Basic	\$ 0.26	\$ 3.39	\$ 0.09	\$ 4.72
Diluted	\$ 0.25	\$ 0.36	\$ 0.06	\$ 0.53
Common shares and equivalents outstanding:				
Basic weighted average shares	20,177	1,777	13,229	1,895
Diluted weighted average shares	20,988	16,788	19,462	16,876

Edgar Filing: ROSETTA STONE INC - Form 10-Q

See accompanying notes to condensed consolidated financial statements.

Table of Contents

ROSETTA STONE INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

Nine Months Ended
September 30,
2009 2008
(unaudited)

CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 1,206	\$ 8,951
Adjustments to reconcile net income to cash provided by operating activities:		
Stock-based compensation expense	21,093	1,140
Bad debt expense	933	849
Depreciation and amortization	3,914	5,224
Write down of deferred financing costs	209	78
Loss on disposal of equipment	40	14
Net change in:		