GLOWPOINT INC
Form 10-Q
May 13, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

ý Quarterly report under Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended March 31, 2008.

or

¨ Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number: 0-25940

GLOWPOINT, INC.
(Exact Name of registrant as Specified in its Charter)

Delaware	**77-0312442**
(State or other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Number)

225 Long Avenue, Hillside, New Jersey 07205
(Address of Principal Executive Offices)

312-235-3888
(Issuer 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 ý 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 definition of accelerated filer, large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	¨	Smaller reporting company	ý

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.)

Yes ¨ No ý

The number of shares outstanding of the registrant s Common Stock as of May 12, 2008 was 46,389,673

GLOWPOINT, INC

Index

PART I FINANCIAL INFORMATION

* The Condensed Consolidated Balance Sheet at December 31, 2007 has been derived from the audited consolidated financial statements filed as an exhibit to our Report on Form 10-K on March 27, 2008.

PART I - FINANCIAL INFORMATION

Item 1

Financial Statements

GLOWPOINT, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except par value and shares)

ASSETS		March 31, 2008 (Unaudited)		December 31, 2007
Current assets:				
Cash and cash equivalents	$	2,112	$	2,312
Accounts receivable, net of allowance for doubtful accounts of $203 and $208; respectively		2,933		2,546
Prepaid expenses and other current assets		314		348
Total current assets		5,359		5,206
Property and equipment, net		2,900		2,692
Other assets		563		664
Total assets	$	8,822	$	8,562
LIABILITIES AND STOCKHOLDERS DEFICIT				
Current liabilities:				
Accounts payable	$	2,127	$	1,575
Accrued expenses		1,289		1,427
Accrued sales taxes and regulatory fees		4,118		4,011
Derivative financial instruments		7,573		6,117
Senior Secured Notes, net of discount of $3,320		7,544		
Senior Secured Notes held by Insider Purchasers related parties, net of discount of $190		267		
Customer deposits		668		713
Deferred revenue		350		330
Current portion of capital lease		134		125
Total current liabilities		24,070		14,298

Long term liabilities:		
Senior Secured Notes, net of discount of $3,912		6,647
Senior Secured Notes held by Insider Purchasers related parties, net of discount of $221		226
Capital lease, less current portion	195	233
Total long term liabilities	195	7,106
Total liabilities	24,265	21,404
Preferred stock, $10,000 par value; 1,500 shares authorized and redeemable; 475 Series C shares issued and outstanding recorded at fair value (stated value and liquidation value of $4,748)	4,330	4,330
Commitments and contingencies		
Stockholders deficit:		
Common stock, $.0001 par value; 150,000,000 and 150,000,000 shares authorized; 47,954,564 and 47,629,564 shares issued; 46,389,673 and 46,064,673 shares outstanding, respectively	5	5
Additional paid-in capital	162,637	162,300
Accumulated deficit	(181,032)	(178,094)
	(18,390)	(15,789)
Less: Treasury stock, 1,564,891 shares at cost	(1,383)	(1,383)
Total stockholders deficit	(19,773)	(17,172)
Total liabilities and stockholders deficit	$ 8,822	$ 8,562

See accompanying notes to condensed consolidated financial statements

1

GLOWPOINT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

(Unaudited)

	Three Months Ended March 31	
	2008	**2007**
Revenue	$ 5,999	$ 5,661
Cost of revenue	3,351	3,916
Gross margin	2,648	1,745
Operating expenses:		
Research and development	238	177
Sales and marketing	879	653
General and administrative	1,894	1,921
Total operating expense	3,011	2,751
Loss from operations	(363)	(1,006)
Interest and other expense (income):		
Interest expense, including $31 and $0, respectively, for Insider Purchasers	1,017	915
Interest income	(11)	(15)
Increase in fair value of derivative financial instruments, including $43 and $0, respectively, for Insider Purchasers	1,456	614
Amortization of deferred financing costs, including $12 and $0, respectively, for Insider Purchasers	113	130
Total interest and other expense, net	2,575	1,644
Net loss	(2,938)	(2,650)
Preferred stock dividends		(85)
Net loss attributable to common stockholders	$ (2,938)	$ (2,735)
Net loss attributable to common stockholders per share:		
Basic and diluted	$ (0.06)	$ (0.06)
Weighted average number of common shares:		
Basic and diluted	46,141	46,540

See accompanying notes to condensed consolidated financial statements

GLOWPOINT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS DEFICIT

Three Months Ended March 31, 2008

(In thousands)

(Unaudited)

	Common Stock		Paid In	Accumulated	Treasury Stock		
	Shares	Amount	Capital	Deficit	Shares	Amount	Total
Balance at January 1, 2008	47,630	$ 5	$ 162,300	$ (178,094)	1,565	$ (1,383)	$ (17,172)
Net loss				(2,938)			(2,938)
Stock-based compensation restricted stock to directors and officers			42				42
Stock-based compensation options to employees			100				100
Stock-based compensation restricted stock for consulting services			16				16
Settlement of accrued 2007 management bonus with restricted stock	325		179				179
Balance at March 31, 2008	47,955	$ 5	$ 162,637	$ (181,032)	1,565	$ (1,383)	$ (19,773)

See accompanying notes to condensed consolidated financial statements

GLOWPOINT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

(Unaudited)

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
Cash flows from Operating Activities:		
Net loss	$ (2,938)	$ (2,650)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	331	429
Other expense recognized for the increase in the estimated fair value of the derivative financial instruments	1,456	614
Amortization of deferred financing costs	113	130
Accretion of discount on Senior Secured Notes	623	628
Beneficial conversion feature for Senior Secured Notes		41
Stock-based compensation	158	145
Increase (decrease) in cash attributable to changes in assets and liabilities:		
Accounts receivable	(387)	398
Prepaid expenses and other current assets	34	(200)
Other assets	(12)	
Accounts payable	552	302
Customer deposits	(45)	227
Accrued expenses, sales taxes and regulatory fees	463	373
Deferred revenue	20	2
Net cash provided by operating activities	368	439
Cash flows from Investing Activities:		
Purchases of property and equipment	(539)	(302)
Net cash used in investing activities	(539)	(302)
Cash flows from Financing Activities:		
Capital lease payments	(29)	
Net cash used in financing activities	(29)	
Increase (decrease) in cash and cash equivalents	(200)	137
Cash and cash equivalents at beginning of period	2,312	2,153
Cash and cash equivalents at end of period	$ 2,112	$ 2,290

Supplement disclosures of cash flow information:				
Cash paid during the period for				
Interest	$	25	$	1
Non-cash investing and financing activities:				
Preferred stock dividends	$		$	85
Additional Senior Secured Notes issued as payment for interest		315		165
Settlement of accrued 2007 management bonus with restricted stock		179		

See accompanying notes to condensed consolidated financial statements

4

GLOWPOINT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2008

(Unaudited)

Note 1 - Basis of Presentation

The Business

Glowpoint, Inc. ("Glowpoint" or "we" or "us" or the Company), a Delaware corporation, is a premiere broadcast-quality, IP (Internet Protocol)-based managed video services provider. Our mission is to improve the ease-of-use, cost-effectiveness, functionality, and quality of existing video communications in order to make it an integral and ubiquitous part of everyday business and personal communications. We believe video communications should be as easy and spontaneous to use as your telephone, but with the power of face-to-face communication. The Company operates in one segment and therefore segment information is not presented.

We view our services as analogous to cellular service providers in the cellular telephone industry. Regardless of the cellular phone purchased, users must select a cellular service provider to make it work. Users make that service decision based on the features, reliability and price offered by the service provider. In our industry, regardless of the video conferencing equipment purchased, Glowpoint provides the managed video services to make it work. In doing so, we offer a vast array of managed video services, including video application services, managed network services, IP and ISDN videoconferencing services, multi-point conferencing (bridging), technology hosting and management, and professional services. In order to address specific needs within an industry, such as broadcast/media content acquisition or retail call center environments, we have bundled some of our managed services to offer unique video communication solutions. We also wholesale some of our services to and provide branding for manufacturers, carriers, and integrators for resale. We provide our managed video services to a wide variety of companies, from global enterprises and large governmental entities to small and medium-sized businesses to other providers of video or telecommunications services. Since its launch in 2000, Glowpoint has been exclusively focused on innovating high quality two-way video communications and has supported millions of video calls. Currently, we support thousands of customer locations in over 1,200 cities in 37 countries around the world.

With the advent of telepresence, we have combined various components of our features and services into a comprehensive video network operations center support service (VNOC Support Service) offering that can support the telepresence systems manufactured by Cisco, Polycom, Tandberg and virtually all other telepresence solutions on the market today. Telepresence is a term to describe high quality, true to life meetings via video communications where participants feel as though they are all sitting in the same physical room even though they may be continents apart. This is accomplished with the use of multiple monitors, special furniture, and strategic camera placement and sound panels to create an immersive experience. We believe that the expensive equipment cost and customer expectations for telepresence demand that a managed service provider, such as Glowpoint, be involved to ensure that all telepresence rooms operate consistently and meetings occur reliably. Given the projected potential market size for these services in the next couple of years, we have focused more resources and time on our VNOC Support Service and related sales opportunities, which sales opportunities tend to be of a larger magnitude than our historical sales opportunities of managed video services.

Liquidity and Going Concern

Our condensed consolidated financial statements have been prepared assuming we will continue as a going concern. We have incurred recurring operating losses and negative operating cash flows since our inception including a net loss attributable to common stockholders of $2,938,000 for the three months ended March 31, 2008. At March 31, 2008, we had a working capital deficit of $18,711,000. We have $2,112,000 in cash and cash equivalents at March 31, 2008 and cash provided by operating activities of $368,000 for the three months ended March 31, 2008. Additionally, the Senior Secured Notes (see Note 6) mature in March 2009. These factors raise substantial doubt as to our ability to continue as a going concern. We raised capital in March and April 2006 and September 2007, but continue to sustain losses and negative operating cash flows. Assuming we are able to negotiate favorable terms with the authorities regarding our sales and use taxes and regulatory fees and assuming we are able to renegotiate or refinance the Senior Secured Notes, we believe that our available capital as of March 31, 2008 will enable us to continue as a going concern through March 31, 2009. There can be no assurances, however that we will be able to raise additional capital as needed or upon acceptable terms nor any assurances that we will be able to renegotiate the terms and maturity date of the Senior Secured Notes. If we are unable to renegotiate the maturity of the Senior Secured Notes or issue new securities on favorable terms to repay them, it would have a material adverse effect on the Company. The accompanying condensed consolidated financial statements do not include any adjustments that might result from this uncertainty.

Summary of Significant Accounting Policies

Quarterly Financial Information and Results of Operations

The condensed consolidated financial statements as of March 31, 2008 and for the three months ended March 31, 2008 and 2007 are unaudited and, in the opinion of management, include all adjustments (consisting only of normal recurring adjustments) necessary to present fairly the financial position as of March 31, 2008, and the results of operations and cash flows for the three months ended March 31, 2008 and 2007. The results for the three months ended March 31, 2008 are not necessarily indicative of the results to be expected for the entire year. While management of the Company believes that the disclosures presented are adequate to make the information not misleading, these condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the footnotes thereto for the fiscal year ended December 31, 2007 as filed with the Securities and Exchange Commission as an exhibit to our Form 10-K on March 27, 2008 (the Audited 2007 Financials).

See Note 2 - Basis of Presentation, Liquidity and Summary of Significant Accounting Policies in the Audited 2007 Financials for a discussion of the estimates and judgments necessary in the Company s accounting for allowance for doubtful accounts, concentration of credit risk, lives of property and equipment, income taxes, stock-based compensation, amortization of deferred financing costs, fair value of financial instruments, derivative financial instruments and accrued sales taxes and regulatory fees. There have been no changes to our critical accounting policies in the three months ended March 31, 2008. Critical accounting policies and the significant estimates made in accordance with them are regularly discussed with our Audit Committee.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of Glowpoint and our wholly owned subsidiary, GP Communications LLC. All material inter-company balances and transactions have been eliminated in consolidation.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current period presentation.

Use of Estimates

Preparation of the condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts could differ from the estimates made. We continually evaluate estimates used in the preparation of the condensed consolidated financial statements for reasonableness. Appropriate adjustments, if any, to the estimates used are made prospectively based upon such periodic evaluation. The significant areas of estimation include determining the allowance for doubtful accounts, deferred tax valuation allowance, accrued sales taxes, regulatory fees and related penalties and interest, the estimated life of customer relationships, the estimated lives and recoverability of property and equipment, the fair value of derivative financial instruments and the valuation of our Series C convertible preferred stock.

Revenue Recognition

We recognize subscription revenue when the related services have been performed. Revenue billed in advance is deferred until the revenue has been earned. Other service revenue, including amounts related to surcharges charged by our carriers, related to the Glowpoint managed network service and the multi-point video and audio bridging services are recognized as service is provided. As the non-refundable, upfront activation fees charged to the subscribers do not meet the criteria as a separate unit of accounting, they are deferred and recognized over the twenty-four month period estimated life of the customer relationship. Revenue related to integration services is recognized at the time the services are performed, and presented in accordance with EITF 99-19 Reporting Revenue Gross as a Principal Versus Net as an Agent . Revenues derived from other sources are recognized when services are provided or events occur.

Long-Lived Assets

We evaluate impairment losses on long-lived assets used in operations, primarily fixed assets, when events and circumstances indicate that the carrying value of the assets might not be recoverable in accordance with Statement of Financial Accounting Standards (SFAS) No. 144 *Accounting for the Impairment or Disposal of Long-Lived Assets* . For purposes of evaluating the recoverability of long-lived assets, the undiscounted cash flows estimated to be generated by those assets are compared to the carrying amounts of those assets. If and when the carrying values of the assets exceed their fair values, the related assets will be written down to fair value. In the three months ended March 31, 2008 and 2007, no impairment losses were indicated or recorded.

Related Party Transactions

The Company receives consulting and tax services from an accounting firm in which one of our directors is a partner and software development from a firm in which one of our other directors is the president. Management believes that such transactions are at arm s-length and for terms that would have been obtained from unaffiliated third parties. For the three months ended March 31, 2008 and 2007, we incurred aggregate fees for these services of $13,000 and $22,000, respectively.

Software Development Costs

The Company incurs costs for the development of its Customer Connect software that is to be sold, leased or licensed to third parties in the future. All software development costs have been appropriately accounted for in accordance with SFAS 86 *Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed* . Software development costs are required to be capitalized when a product s technological feasibility has been established by completion of a detailed program design or working model of the product, and ending when a product is available for release to customers. The Company capitalized $0 and $73,000 of software development costs for the three months ended March 31, 2008 and 2007, respectively. Software development costs of $188,000 are being amortized over 24 months beginning in September 2007, when the product became available for general release to customers and the capitalization of software costs ceased. For the three months ended March 31, 2008 and 2007, we amortized $24,000 and $0, respectively, to cost of revenues. As of March 31, 2008, there was $133,000 of unamortized capitalized software costs. The Company did not capitalize any costs related to the purchase of software and related technologies and content.

Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, *"Fair Value Measurements."* SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements about fair value measurements. SFAS No. 157 was effective for our Company on January 1, 2008. However, in February 2008, the FASB released FASB Staff Position (FSP FAS 157-2 Effective Date of FASB Statement No. 157), which delayed the effective date of SFAS No. 157 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The adoption of SFAS No. 157 for our financial assets and liabilities did not have a material impact on our consolidated financial statements. The Company is currently assessing the impact the adoption of SFAS No. 157 for non-financial assets and liabilities, effective January 1, 2009, will have on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159 *The Fair Value Option for Financial Assets and Financial Liabilities* . SFAS No. 159 permits entities to choose to measure many financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007.

In December 2007, the FASB issued SFAS No. 141 (revised 2007) (SFAS No. 141 (R)), *Business Combinations (SFAS No. 141(R))* . SFAS No. 141(R) revises SFAS No. 141 on establishing the requirements in recognizing and measuring identifiable assets acquired and liabilities assumed within a business combination, any noncontrolling interest, goodwill acquired in a business combination or a gain from a bargain purchase, and any applicable disclosures needed to evaluate the nature and financial effect of a business combination. SFAS No. 141 is effective the first annual reporting period beginning on or after December 15, 2008, and therefore would be effective for the Company beginning January 1, 2009.

In December 2007, the FASB issued SFAS No. 160, (Noncontrolling Interests in Consolidated Financial Statements), an amendment of ARB No. 51 (SFAS No. 160). SFAS 160 amends ARB No. 51 to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary, in which the noncontrolling interest will be reclassified as equity; and the income, expense and comprehensive income from a noncontrolling interest will be fully consolidated. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008, and therefore would be effective for the Company beginning January 1, 2009. The Company is evaluating the impact SFAS 160 will have on its consolidated financial statements.

Note 2 Stock Options

We periodically grant stock options to employees and directors in accordance with the provisions of our stock option plans, with the exercise price of the stock options being set at the closing market price of the common stock on the date of grant. Effective January 1, 2006, the Company adopted Statement of Financial Standards No. 123R, *Share-Based Payment* (SFAS No. 123R) which requires that compensation cost relating to share-based payment transactions be recognized as an expense in the financial statements and that measurement of that cost be based on the estimated fair value of the equity or liability instrument issued. SFAS No. 123R also requires that forfeitures be estimated and recorded over the vesting period of the instrument.

The intrinsic value of options outstanding and exercisable at March 31, 2008 and 2007 was $83,000 and $2,000, respectively. There were no options exercised during the three months ended March 31, 2008.

The remaining unrecognized stock-based compensation expense at March 31, 2008 was $346,000 and will be amortized over a weighted average period of 1.08 years.

The weighted average fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions during the three months ended March 31, 2008 and 2007:

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
Risk free interest rate	3.1%	4.7%
Expected option lives	5 Years	5 Years
Expected volatility	94.5%	99.3%
Estimated forfeiture rate	10%	10%
Expected dividend yields	None	None
Weighted average grant date fair value of options	$ 0.36	$ 0.45

Expected volatility was calculated using the historical volatility of the appropriate industry sector index. The expected term of the options is estimated based on the Company s historical exercise rate and forfeiture rates are estimated based on employment termination experience. The risk free interest rate is based on U.S. Treasury yields for securities in effect at the time of grants with terms approximating the term of the grants. The assumptions used in the Black-Scholes option valuation model are highly subjective, and can materially affect the resulting valuations.

A summary of options granted, exercised, expired and forfeited under our plans and options outstanding as of and for the three months ended March 31, 2008 with respect to all outstanding options is as follows (options in thousands):

	Outstanding		Exercisable	
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
Options outstanding, January 1, 2008	4,213	$ 1.47	2,519	$ 2.06
Granted	149	0.49		
Exercised				
Expired				
Forfeited	(26)	0.66		
Options outstanding, March 31, 2008	4,336	$ 1.44	2,574	$ 2.05