

BSQUARE CORP /WA
Form 10-Q
November 12, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013

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: 000-27687

BSQUARE CORPORATION
(Exact name of registrant as specified in its charter)

Washington
(State or other jurisdiction of
incorporation or organization)

110 110th Avenue NE, Suite 200,

Bellevue WA
(Address of principal executive offices)

(425) 519-5900

91-1650880
(I.R.S. Employer

Identification No.)

98004
(Zip Code)

(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.

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 common stock outstanding as of October 31, 2013: 11,233,580

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FORM 10-Q

For the Quarterly Period Ended September 30, 2013

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****BSQUARE CORPORATION****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share amounts)**

	September 30, 2013 (Unaudited)	December 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 13,236	\$ 9,903
Short-term investments	8,053	9,826
Accounts receivable, net of allowance for doubtful accounts of \$263 at September 30, 2013 and \$200 at December 31, 2012	12,811	16,095
Deferred tax assets	160	296
Prepaid expenses and other current assets	1,300	858
Total current assets	35,560	36,978
Equipment, furniture and leasehold improvements, net	561	759
Restricted cash	250	875
Deferred tax asset	210	2,255
Intangible assets, net	897	1,069
Goodwill	3,738	3,738
Other non-current assets	93	117
Total assets	\$ 41,309	\$ 45,791
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Third-party software fees payable	\$ 11,055	\$ 11,099
Accounts payable	778	553
Accrued compensation	1,986	2,205
Other accrued expenses	1,332	1,732
Deferred revenue	1,074	837
Total current liabilities	16,225	16,426
Deferred tax liability	206	206
Deferred rent	422	154
Shareholders equity:		

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Preferred stock, no par value: 10,000,000 shares authorized; no shares issued and outstanding		
Common stock, no par value: 37,500,000 shares authorized; 11,203,707 shares issued and outstanding at September 30, 2013 and 11,065,217 shares issued and outstanding at December 31, 2012	129,215	128,474
Accumulated other comprehensive loss	(791)	(733)
Accumulated deficit	(103,968)	(98,736)
Total shareholders equity	24,456	29,005
Total liabilities and shareholders equity	\$ 41,309	\$ 45,791

See notes to condensed consolidated financial statements.

Table of Contents**BSQUARE CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS****(In thousands, except per share amounts) (Unaudited)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Revenue:				
Software	\$ 18,456	\$ 19,635	\$ 51,818	\$ 55,645
Service	5,116	5,850	14,461	19,893
Total revenue	23,572	25,485	66,279	75,538
Cost of revenue:				
Software	15,965	15,730	43,087	45,094
Service	4,238	4,913	12,683	16,410
Total cost of revenue	20,203	20,643	55,770	61,504
Gross profit	3,369	4,842	10,509	14,034
Operating expenses:				
Selling, general and administrative	3,960	2,866	11,432	10,557
Research and development	804	861	2,205	2,909
Total operating expenses	4,764	3,727	13,637	13,466
Income (loss) from operations	(1,395)	1,115	(3,128)	568
Other income (expense), net	(15)	28	100	122
Income (loss) before income taxes	(1,410)	1,143	(3,028)	690
Income tax expense	(2,157)	(533)	(2,206)	(470)
Net income (loss)	\$ (3,567)	\$ 610	\$ (5,234)	\$ 220
Basic income (loss) per share	\$ (0.32)	\$ 0.06	\$ (0.47)	\$ 0.02
Diluted income (loss) per share	\$ (0.32)	\$ 0.05	\$ (0.47)	\$ 0.02
Shares used in calculation of income (loss) per share:				
Basic	11,194	10,943	11,150	10,935
Diluted	11,194	11,474	11,150	11,450

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Comprehensive income (loss):				
Net income (loss)	\$ (3,567)	\$ 610	\$ (5,234)	\$ 220
Other comprehensive income (expense):				
Foreign currency translation, net of tax	56	(65)	(35)	(75)
Change in unrealized gains on investments, net of tax	1	6	(2)	18
Total other comprehensive income (expense)	57	(59)	(37)	(57)
Comprehensive income (loss)	\$ (3,510)	\$ 551	\$ (5,271)	\$ 163

See notes to condensed consolidated financial statements.

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BSQUARE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands) (Unaudited)

	Nine Months Ended	
	September 30,	
	2013	2012
Cash flows from operating activities:		
Net loss	\$ (5,234)	\$ 220
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	586	758
Stock-based compensation	726	685
Deferred income taxes	2,181	415
Changes in operating assets and liabilities:		
Accounts receivable, net	3,284	(3,176)
Prepaid expenses and other assets	(418)	367
Third-party software fees payable	(44)	2,303
Accounts payable and accrued expenses	(394)	(1,076)
Deferred revenue	237	331
Deferred rent	268	(13)
Net cash provided by operating activities	1,192	814
Cash flows from investing activities:		
Purchases of equipment and furniture	(216)	(336)
Proceeds from maturities of short-term investments	8,932	8,400
Purchases of short-term investments	(7,163)	(10,535)
Reduction of restricted cash	625	
Net cash provided by (used in) investing activities	2,178	(2,471)
Cash flows provided by financing activities		
proceeds from exercise of stock options	12	193
Effect of exchange rate changes on cash	(49)	(144)
Net increase (decrease) in cash and cash equivalents	3,333	(1,608)
Cash and cash equivalents, beginning of period	9,903	8,505
Cash and cash equivalents, end of period	\$ 13,236	\$ 6,897

See notes to condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2013

(Unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of BSQUARE Corporation (**BSQUARE**) have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (**SEC**) for interim financial reporting and include the accounts of BSQUARE and our wholly owned subsidiaries. Certain information and footnote disclosures normally included in the annual consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles (**GAAP**) have been condensed or omitted pursuant to such rules and regulations. In our opinion, the unaudited condensed consolidated financial statements include all material adjustments, all of which are of a normal and recurring nature, necessary to present fairly our financial position as of September 30, 2013 and our operating results and cash flows for the three and nine months ended September 30, 2013 and 2012. The accompanying financial information as of December 31, 2012 is derived from audited financial statements. Preparing financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. Examples include provisions for bad debts and income taxes, estimates of progress on professional engineering service arrangements and bonus accruals. Actual results may differ from these estimates. Interim results are not necessarily indicative of results for a full year. The information included in this Quarterly Report on Form 10-Q should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2012. All intercompany balances have been eliminated.

Recently Issued Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (**FASB**) issued an accounting standard update (**ASU**) No. 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. Under ASU 2013-02, an entity is required to provide information about the amounts reclassified out of Accumulated Other Comprehensive Income (**AOCI**) by component. In addition, an entity is required to present, either on the face of the financial statements or in the notes, significant amounts reclassified out of AOCI by the respective line items of net income, but only if the amount reclassified is required to be reclassified in its entirety in the same reporting period. For amounts that are not required to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures that provide additional details about those amounts. ASU 2013-02 does not change the current requirements for reporting net income or other comprehensive income in the financial statements. Our adoption of ASU 2013-02 effective January 1, 2013 did not have any effect on our financial position, results of operations or cash flows.

Income (Loss) Per Share

Basic income or loss per share is computed using the weighted average number of common shares outstanding during the period, and excludes any dilutive effects of common stock equivalent shares, such as options, restricted stock awards and restricted stock units. Restricted stock awards (**RSAs**) are considered outstanding and included in the computation of basic income or loss per share when underlying restrictions expire and the awards are no longer

forfeitable. Restricted stock units (RSUs) are considered outstanding and included in the computation of basic income or loss per share only when vested. Diluted income per share is computed using the weighted average number of common shares outstanding and common stock equivalent shares outstanding during the period using the treasury stock method.

Common stock equivalent shares of 940,812 and 837,812 and 993,687 and 904,637 were excluded from the computations of basic and diluted income per share for the three and nine months ended September 30, 2013 and 2012, respectively,, because their effect was anti-dilutive. Unvested but outstanding RSUs and RSAs which are forfeitable are included in the diluted income per share calculation. In a period where we are in a net loss position, the diluted loss per share is computed using the basic share count.

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Cash, cash equivalents, short-term investments, and restricted cash consisted of the following at September 30, 2013 and December 31, 2012 (in thousands):

	September 30, 2013	December 31, 2012
Cash	\$ 3,297	\$ 2,590
Cash equivalents money market fund	9,939	7,313
Total cash and cash equivalents	13,236	9,903
Short-term investments:		
Municipal securities		356
Corporate commercial paper	1,250	4,374
Foreign government bonds	1,001	999
Corporate debt securities	5,802	4,097
Total short-term investments	8,053	9,826
Restricted cash money market fund	250	875
Total cash, cash equivalents, short-term investments and restricted cash	\$ 21,539	\$ 20,604

Gross unrealized gains and losses on our short-term investments were not material as of September 30, 2013 and December 31, 2012. Our restricted cash balance at September 30, 2013 and December 31, 2012 relates to a letter of credit which secures our corporate headquarters lease.

3. Fair Value Measurements

We measure our cash equivalents and short-term investments at fair value. Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability. A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value:

- Level 1: Quoted prices in active markets for identical assets or liabilities.
- Level 2: Directly or indirectly observable market-based inputs or unobservable inputs used in models or other valuation methodologies.
- Level 3: Unobservable inputs that are not corroborated by market data. The inputs require significant management judgment or estimation.

We classify our cash equivalents and short-term investments within Level 1 or Level 2 because our cash equivalents and short-term investments are valued using quoted market prices or alternative pricing sources and models utilizing market observable inputs.

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Assets and liabilities measured at fair value on a recurring basis as of September 30, 2013 and December 31, 2012 are summarized below (in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Direct or Indirect Observable Inputs (Level 2)	Total
Assets:			
Cash equivalents money market fund	\$ 9,939	\$	\$ 9,939
Short-term investments:			
Corporate commercial paper		1,250	1,250
Foreign government bonds		1,001	1,001
Corporate debt securities		5,802	5,802
Total short-term investments		8,053	8,053
Restricted cash money market fund	250		