

SPS COMMERCE INC
Form 10-Q
July 31, 2014
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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: June 30, 2014

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 001-34702

SPS COMMERCE, INC.

(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or Other Jurisdiction of

41-2015127
(I.R.S. Employer

Incorporation or Organization)

Identification No.)

333 South Seventh Street, Suite 1000, Minneapolis, MN 55402

(Address of Principal Executive Offices, Including Zip Code)

(612) 435-9400

(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 (§229.405 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.

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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, par value \$0.001 per share, outstanding at July 24, 2014 was 16,234,758 shares.

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This Quarterly Report on Form 10-Q contains forward-looking statements regarding us, our business prospects and our results of operations that are subject to certain risks and uncertainties posed by many factors and events that could cause our actual business, prospects and results of operations to differ materially from those that may be anticipated by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those described under the heading *Risk Factors* included in our Annual Report on Form 10-K for the year ended December 31, 2013 as filed with the Securities and Exchange Commission. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this report. We expressly disclaim any intent or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Readers are urged to carefully review and consider the various disclosures

made by us in this report and in our other reports filed with the Commission that advise interested parties of the risks and factors that may affect our business.

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****SPS COMMERCE, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

(Unaudited; in thousands, except share amounts)

| | June 30, 2014 | December 31, 2013 |
|--|--------------------------|------------------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 136,508 | \$ 131,294 |
| Accounts receivable, less allowance for doubtful accounts of \$242 and \$237, respectively | 13,348 | 11,611 |
| Deferred costs, current | 10,415 | 9,048 |
| Deferred income taxes, current | 1,272 | 1,272 |
| Prepaid expenses and other current assets | 3,346 | 2,850 |
| Total current assets | 164,889 | 156,075 |
| PROPERTY AND EQUIPMENT, net | 9,036 | 9,922 |
| GOODWILL | 25,487 | 25,487 |
| INTANGIBLE ASSETS, net | 15,683 | 17,082 |
| OTHER ASSETS | | |
| Deferred costs, net of current portion | 4,578 | 3,684 |
| Deferred income taxes, net of current portion | 10,294 | 10,870 |
| Other non-current assets | 205 | 210 |
| | \$ 230,172 | \$ 223,330 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 2,999 | \$ 1,798 |
| Accrued compensation and benefits | 7,639 | 7,981 |
| Accrued expenses and other current liabilities | 1,805 | 2,801 |
| Deferred revenue, current | 6,912 | 6,335 |
| Total current liabilities | 19,355 | 18,915 |
| OTHER LIABILITIES | | |
| Deferred revenue, less current portion | 10,017 | 8,785 |
| Deferred rent | 2,663 | 2,857 |
| Total liabilities | 32,035 | 30,557 |

COMMITMENTS and CONTINGENCIES

STOCKHOLDERS EQUITY

| | | |
|--|------------|------------|
| Preferred stock, \$0.001 par value; 5,000,000 shares authorized; 0 shares issued and outstanding | | |
| Common stock, \$0.001 par value; 55,000,000 shares authorized; 16,230,057 and 16,092,121 shares issued and outstanding, respectively | 16 | 16 |
| Additional paid-in capital | 243,901 | 239,549 |
| Accumulated deficit | (45,780) | (46,792) |
| Total stockholders equity | 198,137 | 192,773 |
| | \$ 230,172 | \$ 223,330 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

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SPS COMMERCE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited; in thousands, except per share amounts)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|-----------------------------------|-----------|------------------------------|-----------|
| | 2014 | 2013 | 2014 | 2013 |
| Revenues | \$ 31,100 | \$ 25,658 | \$ 60,039 | \$ 49,410 |
| Cost of revenues | 9,627 | 7,943 | 18,882 | 15,009 |
| Gross profit | 21,473 | 17,715 | 41,157 | 34,401 |
| Operating expenses | | | | |
| Sales and marketing | 11,570 | 9,647 | 22,454 | 18,872 |
| Research and development | 3,365 | 2,657 | 6,339 | 5,160 |
| General and administrative | 4,842 | 4,211 | 9,353 | 8,258 |
| Amortization of intangible assets | 682 | 717 | 1,399 | 1,434 |
| Total operating expenses | 20,459 | 17,232 | 39,545 | 33,724 |
| Income from operations | 1,014 | 483 | 1,612 | 677 |
| Other income (expense) | | | | |
| Interest income | 50 | 22 | 99 | 45 |
| Other income (expense), net | 35 | (48) | (21) | (132) |
| Total other income (expense), net | 85 | (26) | 78 | (87) |
| Income before income taxes | 1,099 | 457 | 1,690 | 590 |
| Income tax expense | (460) | (169) | (678) | (103) |
| Net income | \$ 639 | \$ 288 | \$ 1,012 | \$ 487 |
| Net income per share | | | | |
| Basic | \$ 0.04 | \$ 0.02 | \$ 0.06 | \$ 0.03 |
| Diluted | \$ 0.04 | \$ 0.02 | \$ 0.06 | \$ 0.03 |
| Weighted average common shares used to compute net income per share | | | | |
| Basic | 16,210 | 15,076 | 16,183 | 14,983 |
| Diluted | 16,768 | 15,785 | 16,799 | 15,677 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

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SPS COMMERCE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited; in thousands)

| | Six Months Ended June 30, | |
|---|--------------------------------------|-------------|
| | 2014 | 2013 |
| Cash flows from operating activities | | |
| Net income | \$ 1,012 | \$ 487 |
| Reconciliation of net income to net cash provided by operating activities | | |
| Deferred income taxes | 576 | 31 |
| Depreciation and amortization of property and equipment | 2,823 | 2,353 |
| Amortization of intangible assets | 1,399 | 1,434 |
| Provision for doubtful accounts | 323 | 185 |
| Stock-based compensation | 2,698 | 2,035 |
| Changes in assets and liabilities | | |
| Accounts receivable | (2,060) | (951) |
| Deferred costs | (2,260) | (1,265) |
| Prepaid expenses and other current assets | (491) | 2,512 |
| Accounts payable | 1,202 | (207) |
| Accrued compensation and benefits | (342) | 473 |
| Accrued expenses and other current liabilities | 421 | 497 |
| Deferred rent | (170) | |
| Deferred revenue | 1,809 | 1,049 |
| Net cash provided by operating activities | 6,940 | 8,633 |
| Cash flows from investing activities | | |
| Purchases of property and equipment | (3,380) | (1,737) |
| Net cash used in investing activities | (3,380) | (1,737) |
| Cash flows from financing activities | | |
| Net proceeds from exercise of options to purchase common stock | 922 | 1,597 |
| Excess tax benefit from exercise of options to purchase common stock | 60 | 40 |
| Net proceeds from employee stock purchase plan | 672 | 551 |
| Net cash provided by financing activities | 1,654 | 2,188 |
| Net increase in cash and cash equivalents | 5,214 | 9,084 |
| Cash and cash equivalents at beginning of period | 131,294 | 66,050 |
| Cash and cash equivalents at end of period | \$ 136,508 | \$ 75,134 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

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SPS COMMERCE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

NOTE A General

Business Description

We are a leading provider of cloud-based supply chain management solutions, providing prewired, proven integrations and comprehensive retail performance analytics to thousands of customers worldwide. We provide our solutions through the SPS Commerce platform, a cloud-based software suite that improves the way suppliers, retailers, distributors and other customers manage and fulfill orders. We derive the majority of our revenues from thousands of monthly recurring subscriptions from businesses that utilize our solutions.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of SPS Commerce, Inc. and its subsidiaries. All intercompany accounts and transactions have been eliminated in the condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, these condensed consolidated financial statements do not include all of the information and notes required by GAAP. We have included all normal recurring adjustments considered necessary to give a fair statement of our financial position, results of operations and cash flows for the interim periods shown. Operating results for these interim periods are not necessarily indicative of the results to be expected for the full year. The December 31, 2013 condensed consolidated balance sheet data was derived from our audited financial statements at that date. For further information, refer to the consolidated financial statements and accompanying notes for the year ended December 31, 2013 included in our Annual Report on Form 10-K as filed with the Securities and Exchange Commission on February 20, 2014.

Use of Estimates

Preparing financial statements in conformity with GAAP 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 financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Significant Accounting Policies

During the six months ended June 30, 2014, there were no material changes in our significant accounting policies. See Note A to the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2013, as filed with the Securities and Exchange Commission on February 20, 2014, for additional information regarding our significant accounting policies.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board issued new accounting requirements for the recognition of revenue from contracts with customers. These new requirements are effective for annual reporting periods beginning after December 15, 2016, and interim periods within those annual periods. We are currently evaluating the impact of

this guidance on our results of operations and financial position.

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There was no change in our goodwill for the six months ended June 30, 2014.

Intangible assets included the following (in thousands):

| | June 30, 2014 | | | December 31, 2013 | | |
|----------------------------|-----------------|--------------------------|-----------|-------------------|--------------------------|-----------|
| | Carrying Amount | Accumulated Amortization | Net | Carrying Amount | Accumulated Amortization | Net |
| Subscriber relationships | \$ 23,160 | \$ (7,638) | \$ 15,522 | \$ 23,160 | \$ (6,376) | \$ 16,784 |
| Non-competition agreements | 1,710 | (1,549) | 161 | 1,710 | (1,412) | 298 |
| | \$ 24,870 | \$ (9,187) | \$ 15,683 | \$ 24,870 | \$ (7,788) | \$ 17,082 |

Amortization expense for intangible assets was \$682,000 and \$1.4 million for the three and six months ended June 30, 2014, and \$717,000 and \$1.4 million for the three and six months ended June 30, 2013, respectively.

At June 30, 2014, future amortization expense for intangible assets was as follows (in thousands):

| | |
|-------------------|-----------|
| Remainder of 2014 | \$ 1,288 |
| 2015 | 2,578 |
| 2016 | 2,578 |
| 2017 | 2,557 |
| 2018 | 2,062 |
| Thereafter | 4,620 |
| | \$ 15,683 |

NOTE C Line of Credit

We have a revolving credit agreement with JPMorgan Chase Bank, N.A. which provides for a \$20 million revolving credit facility that we may draw upon from time to time, subject to certain terms and conditions, and will mature on September 30, 2016.

There were no borrowings outstanding at June 30, 2014 and we were in compliance with all covenants under the revolving credit agreement as of that date.

NOTE D Stock-Based Compensation

Our equity compensation plans provide for the grant of incentive and nonqualified stock options, as well as other stock-based awards including restricted stock and restricted stock units, to employees, non-employee directors and other consultants who provide services to us. Restricted stock awards result in the issuance of new shares when granted. For other stock-based awards, new shares are issued when the award is exercised, vested or released according to the terms of the agreement. In January 2014, 965,527 additional shares were reserved for future issuance

under our 2010 Equity Incentive Plan. At June 30, 2014, there were approximately 2.6 million shares available for grant under approved equity compensation plans.

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We recorded non-cash stock-based compensation expense of \$1.4 million and \$2.7 million for the three and six months ended June 30, 2014, and \$1.1 million and \$2.0 million for the three and six months ended June 30, 2013, respectively. This expense was allocated as follows (in thousands):

| | Three Months Ended | | Six Months | |
|---------------------|--------------------|--------|------------|--------|
| | June 30, | | Ended | |
| | 2014 | 2013 | 2014 | 2013 |
| Cost of revenues | \$ 152 | \$ 122 | \$ 305 | \$ 225 |
| Operating expenses | | | | |
| Sales and marketing | 472 | | | |