Monotype Imaging Holdings Inc.
Form 10-Q
July 29, 2015
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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 June 30, 2015

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 001-33612

MONOTYPE IMAGING HOLDINGS INC.

(Exact name of registrant as specified in its charter)

Delaware	**20-3289482**
(State of incorporation)	**(I.R.S. Employer Identification No.)**
600 Unicorn Park Drive	
Woburn, Massachusetts	**01801**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (781) 970-6000

(Former Name, Former Address and Former Fiscal year, if changed since last report)

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 x 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 x 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 x	Accelerated filer ¨
Non-accelerated filer ¨	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 x

The number of shares outstanding of the registrant s common stock as of July 22, 2015 was 39,753,358.

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MONOTYPE IMAGING HOLDINGS INC.

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

MONOTYPE IMAGING HOLDINGS INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited and in thousands, except share and per share data)

	June 30, 2015	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$ 74,620	$ 90,325
Accounts receivable, net of allowance for doubtful accounts of $205 at June 30, 2015 and $164 at December 31, 2014	10,085	9,279
Income tax refunds receivable	2,925	2,593
Deferred income taxes	2,763	2,898
Prepaid expenses and other current assets	3,734	4,361
Total current assets	94,127	109,456
Property and equipment, net	15,611	10,578
Goodwill	187,194	176,999
Intangible assets, net	73,556	73,862
Other assets	1,836	3,563
Total assets	$ 372,324	$ 374,458
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 504	$ 1,156
Accrued expenses and other current liabilities	18,088	24,570
Accrued income taxes payable	477	640
Deferred revenue	8,303	7,107
Total current liabilities	27,372	33,473
Other long-term liabilities	3,274	2,596
Contingent acquisition consideration	4,997	
Deferred income taxes	35,024	32,960
Reserve for income taxes	3,044	4,637
Accrued pension benefits	5,361	5,679
Commitments and contingencies *(Note 15)*		
Stockholders equity:		

Preferred stock, $0.001 par value, Authorized shares: 10,000,000; Issued and outstanding: none		
Common stock, $0.001 par value, Authorized shares: 250,000,000; Issued: 41,701,482 at June 30, 2015 and 40,770,197 at December 31, 2014	41	39
Additional paid-in capital	246,424	232,522
Treasury stock, at cost, 1,982,364 shares at June 30, 2015 and 1,303,737 shares at December 31, 2014	(50,455)	(31,946)
Retained earnings	103,962	98,672
Accumulated other comprehensive loss	(6,720)	(4,174)
Total stockholders equity	293,252	295,113
Total liabilities and stockholders equity	$ 372,324	$ 374,458

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

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MONOTYPE IMAGING HOLDINGS INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited and in thousands, except share and per share data)

	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014	Six Months Ended June 30, 2015	Six Months Ended June 30, 2014
Revenue	$ 46,405	$ 44,963	$ 92,451	$ 91,035
Cost of revenue	7,553	7,322	14,963	13,830
Cost of revenue amortization of acquired technology	1,134	1,146	2,267	2,291
Total cost of revenue	8,687	8,468	17,230	16,121
Gross profit	37,718	36,495	75,221	74,914
Operating expenses:				
Marketing and selling	14,532	11,987	27,508	23,105
Research and development	5,290	4,910	11,089	10,663
General and administrative	7,010	5,386	13,909	11,584
Amortization of other intangible assets	790	1,431	1,492	2,863
Total operating expenses	27,622	23,714	53,998	48,215
Income from operations	10,096	12,781	21,223	26,699
Other (income) expense:				
Interest expense	449	256	795	534
Interest income	(145)	(6)	(257)	(8)
Loss on foreign exchange	498	136	612	170
Loss on derivatives	208	158	72	214
Other income, net	(1)	(3)	(2)	(4)
Total other expense	1,009	541	1,220	906
Income before provision for income taxes	9,087	12,240	20,003	25,793
Provision for income taxes	3,183	4,549	6,742	9,657
Net income	$ 5,904	$ 7,691	$ 13,261	$ 16,136
Net income available to common stockholders basic	$ 5,754	$ 7,532	$ 12,960	$ 15,847
Net income available to common stockholders diluted	$ 5,755	$ 7,534	$ 12,962	$ 15,847

Net income per common share:								
Basic	$	0.15	$	0.19	$	0.33	$	0.41
Diluted	$	0.15	$	0.19	$	0.33	$	0.40
Weighted-average number of shares outstanding:								
Basic		38,826,185		38,714,178		38,827,668		38,713,432
Diluted		39,395,395		39,623,517		39,458,758		39,865,906
Dividends declared per common share	$	0.10	$	0.08	$	0.20	$	0.16

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

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MONOTYPE IMAGING HOLDINGS INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited and in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Net income	$ 5,904	$ 7,691	$ 13,261	$ 16,136
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	1,560	(166)	(2,546)	(161)
Comprehensive income	$ 7,464	$ 7,525	$ 10,715	$ 15,975

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

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MONOTYPE IMAGING HOLDINGS INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited and in thousands)

	Six Months Ended June 30,	
	2015	**2014**
Cash flows from operating activities		
Net income	$ 13,261	$ 16,136
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,096	5,970
Loss on retirement of fixed assets	20	9
Amortization of deferred financing costs and accreted interest	258	227
Adjustment to contingent consideration		(552)
Share based compensation	6,241	5,016
Excess tax benefit on stock options	(1,726)	(1,951)
Provision for doubtful accounts	105	
Deferred income taxes	2,317	1,772
Unrealized currency loss (gain) on foreign denominated intercompany transactions	13	(140)
Changes in operating assets and liabilities:		
Accounts receivable	(737)	(1,039)
Prepaid expenses and other assets	2,186	353
Accounts payable	(623)	405
Accrued income taxes payable	(131)	4,614
Accrued expenses and other liabilities	(3,164)	(2,540)
Deferred revenue	1,247	1,920
Net cash provided by operating activities	24,363	30,200
Cash flows from investing activities		
Purchases of property and equipment	(6,847)	(2,472)
Acquisition of business, net of cash acquired	(14,289)	(1,015)
Net cash used in investing activities	(21,136)	(3,487)
Cash flows from financing activities		
Excess tax benefit on stock options	1,726	1,951
Common stock dividends paid	(7,156)	(5,528)
Purchase of treasury stock	(18,601)	(23,881)
Payment of contingent consideration	(289)	
Proceeds from exercises of common stock options	5,854	3,111
Net cash used in financing activities	(18,466)	(24,347)
Effect of exchange rates on cash and cash equivalents	(466)	27

(Decrease) increase in cash and cash equivalents	(15,705)	2,393
Cash and cash equivalents at beginning of period	90,325	78,411
Cash and cash equivalents at end of period	$ 74,620	$ 80,804

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

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MONOTYPE IMAGING HOLDINGS INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2015

1. Nature of the Business

Monotype Imaging Holdings Inc. (the Company or we) is a leading provider of type, technology and expertise for creative applications and consumer devices. Our end-user and embedded solutions for print, web and mobile environments enable people to create and consume dynamic content on any and every device. Our technologies and fonts enable the display and printing of high quality digital text. Our technologies and fonts have been widely deployed across, and embedded in, a range of consumer devices including laser printers, digital copiers, mobile phones, e-book readers, tablets, automotive displays, digital cameras, navigation devices, digital televisions, set-top boxes and consumer appliances, as well as in numerous software applications and operating systems. We also provide printer drivers, page description language interpreters, printer user interface technology and color imaging solutions to printer manufacturers and OEMs (original equipment manufacturers). We license our fonts and technologies to consumer device manufacturers, independent software vendors and creative and business professionals and we are headquartered in Woburn, Massachusetts. We operate in one business segment: the development, marketing and licensing of technologies and fonts. We also maintain various offices worldwide for selling and marketing, research and development and administration. We conduct our operations through four domestic operating subsidiaries, Monotype Imaging Inc., Monotype ITC Inc., MyFonts Inc. and Swyft Media Inc., and five foreign operating subsidiaries, Monotype Ltd., Monotype GmbH and its wholly-owned subsidiary, FontShop International Inc., Monotype Solutions India Pvt. Ltd., Monotype Hong Kong Ltd. and Monotype KK.

2. Basis of Presentation

The accompanying unaudited condensed consolidated interim financial statements as of June 30, 2015 and for the three and six months ended June 30, 2015 and 2014 include the accounts of the Company and its wholly-owned subsidiaries and have been prepared in conformity with accounting principles generally accepted in the United States (GAAP) for interim financial reporting and pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) for Quarterly Reports on Form 10-Q and Article 10 of Regulation S-X. Accordingly, such financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. GAAP requires the Company s management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates. The results for interim periods are not necessarily indicative of results to be expected for the year or for any future periods.

In management s opinion, these unaudited condensed consolidated interim financial statements contain all adjustments of a normal recurring nature necessary for a fair presentation of the financial statements for the interim periods presented.

These unaudited condensed consolidated interim financial statements should be read in conjunction with the Company s audited consolidated financial statements for the year ended December 31, 2014 as reported in the Company s Annual Report on Form 10-K.

The accompanying condensed consolidated financial statements reflect the application of certain significant accounting policies as described below and elsewhere in these notes to the condensed consolidated financial statements. As of June 30, 2015, the Company s significant accounting policies and estimates, which are detailed in the

Company s Annual Report on Form 10-K for the year ended December 31, 2014, have not changed.

3. Recent Accounting Pronouncements

Internal-Use Software

In April 2015, the Financial Accounting Standards Board, or FASB issued ASU 2015-05, *Intangibles Goodwill and Other Internal-Use Software (Subtopic 350-40), Customer s Accounting for Fees Paid in a Cloud Computing Arrangement.* ASU 2015-05 provides guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The guidance will not change GAAP for a customer s accounting for service contracts. The ASU aims to reduce complexity and diversity in practice. The standard is effective for the Company on January 1, 2016, with early adoption permitted. The Company is currently evaluating the impact of the adoption of ASU 2015-03 on its consolidated financial statements.

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Interest

In April 2015, the FASB, issued ASU 2015-03, *Interest Imputation of Interest (Subtopic 835-30), Simplifying the Presentation of Debt Issuance Costs,* which provides that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct reduction from the carrying amount of the related debt liability, rather than classifying the costs separately in the balance sheet as a deferred charge. The ASU aims to reduce complexity. The standard is effective for the Company on January 1, 2017. The Company is currently evaluating the impact of the adoption of ASU 2015-03 on its consolidated financial statements, but does not expect the adoption of this standard to have any impact.

Consolidation

In February 2015, the FASB issued updated accounting guidance on consolidation requirements. This update changes the guidance with respect to the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. This guidance is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2015, with early adoption permitted. The Company does not expect adoption of this guidance to have a material impact on our financial statements.

Going Concern

In August 2014, the FASB issued ASU 2014-15, *Presentation of Financial Statements Going Concern (Subtopic 205-40); Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern*, which requires management of a company to evaluate whether there is substantial doubt about the company s ability to continue as a going concern. The ASU provides guidance on evaluating an entity s ability to continue as a going concern and the content of any required footnote disclosure based on that evaluation. The assessment period is one year after the date of the financial statements are issued. The standard is effective for the Company on January 1, 2017. Early adoption is permitted. The Company is currently evaluating the impact of the adoption of ASU 2014-15, but we do not expect the adoption of this standard to have any impact on its consolidated financial statements.

Revenue Recognition

In May 2014, the FASB and the International Accounting Standards Board jointly issued ASU 2014-9, *Revenue from Contracts with Customers (Topic 606),* which provides a comprehensive new revenue recognition model that requires revenue to be recognized in a manner to depict the transfer of goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services. This guidance was effective for annual reporting and interim periods beginning after December 15, 2016 and allows for either full retrospective or modified retrospective application, with early adoption not permitted. On July 9, 2015 the FASB voted to approve a one-year deferral of the effective date of this guidance. In accordance with the agreed upon delay, the guidance is effective for the Company on January 1, 2018. The Company is currently evaluating the adoption method it will apply and the impact that this guidance will have on its financial statements and related disclosures.

4. Acquisitions

Swyft Media

On January 30, 2015, the Company purchased all of the outstanding stock of TextPride, Inc. operating under the name of Swyft Media, a privately-held mobile messaging company located in New York, New York. In connection with the acquisition, TextPride, Inc. was renamed Swyft Media Inc. and became a wholly-owned subsidiary of the registrant.

Swyft Media s expertise in the emerging world of branded, in-app mobile messaging content is expected to help Monotype reach new customers, with an opportunity to add value by including some of the world s largest and most popular collections of fonts. The impact of this acquisition was not material to our condensed consolidated financial statements.

The Company acquired Swyft Media for an aggregate purchase price of approximately $17.0 million, consisting of $12.1 million in cash, plus contingent consideration of up to $15.0 million payable through 2018, which had an estimated net present value of $4.9 million. We paid $11.6 million from cash on hand at the time of the acquisition, net of cash acquired. Of the purchase price, approximately $4.7 million and $13.6 million have been allocated to intangible assets and goodwill, respectively. The fair value of the assets acquired and liabilities assumed is less than the purchase price, resulting in the recognition of goodwill. The goodwill reflects the value of the synergies we expect to realize and the assembled workforce. The acquisition of Swyft Media was structured in such a manner that the goodwill is not expected to be deductible for tax purposes. The purchase price has been allocated to the tangible and intangible assets acquired and liabilities assumed based upon the respective estimates of fair value as of the date of the acquisition, which remains preliminary as of June 30, 2015, and using assumptions that the Company s management believes are reasonable given the information currently available. The final allocation of the purchase price to intangible assets, goodwill and deferred tax assets and liabilities may differ materially from the information presented in these condensed consolidated financial statements. Twelve

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employees joined the Company in connection with the acquisition. See Note 6 for additional information on the fair value measurements for all financial assets and liabilities, including contingent consideration, which is measured at fair value on a recurring basis.

FontShop

On July 14, 2014, the Company purchased all of the outstanding stock of FontShop International GmbH, a privately-held font distributor located in Berlin, Germany, its wholly-owned subsidiary FontShop International, Inc. based in San Francisco, California, the FontFont typeface library, FontShop AG of Berlin, the largest distributor of the FontFont library, and certain other typeface families, collectively FontShop, for an aggregate purchase price of $14.6 million. We paid $11.9 million from cash on hand at the time of the acquisition, and the remainder, or $2.7 million, was paid in January 2015. Of the final purchase price, $8.5 million and $6.3 million was allocated to intangible assets and goodwill, respectively. The purchase price allocation was finalized as of June 30, 2015. Approximately $6.3 million of the goodwill is expected to be deductible for tax purposes. The purchase price was allocated to the tangible and intangible assets acquired and liabilities assumed based upon the respective estimates of fair value as of the date of the acquisition, and using assumptions that the Company s management believes are reasonable given the information that was currently available. On October 9, 2014, FontShop International GmbH was merged into Monotype Germany effective August 1, 2014. Following the merger, FontShop International Inc. became a wholly-owned subsidiary of Monotype Germany. On October 28, 2014, FontShop AG was merged into Monotype Germany. Fifty employees joined the Company in connection with the acquisition.

5. Derivative Financial Instruments

We incur foreign currency exchange gains and losses related to certain customers that are invoiced in U.S. dollars, but who have the option to make an equivalent payment in their own functional currencies at a specified exchange rate as of a specified date. In the period from that date until payment in the customer s functional currency is received and converted into U.S. dollars, we can incur realized gains and losses. We also incur foreign currency exchange gains and losses on certain intercompany assets and liabilities denominated in foreign currencies. We are currently utilizing 30-day forward contracts to mitigate our exposure on these currency fluctuations. These contracts are generally set to expire and are settled at month end. The instruments are not designated as hedging instruments, and accordingly, the gain or loss is recognized upon cash settlement and is included in loss on derivatives in the accompanying condensed consolidated statements of income. At June 30, 2015 and December 31, 2014 we had one forward foreign exchange contract outstanding, which was entered into on those dates. See Note 6 for details regarding the fair value of these instruments.

The following table presents the losses on our derivative financial instruments which are included in loss on derivatives in our accompanying condensed consolidated statements of income (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Currency swaps	$ 208	$ 158	$ 72	$ 214
Total	$ 208	$ 158	$ 72	$ 214

6. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, the Codification established a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Other inputs that are observable directly or indirectly, such as quoted prices for similar assets and liabilities or market corroborated inputs.

Level 3: Unobservable inputs are used when little or no market data is available and requires the company to develop its own assumptions about how market participants would price the assets or liabilities. The fair value hierarchy gives the lowest priority to Level 3 inputs.

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In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimizes the use of unobservable inputs to the extent possible as well as considers counterparty and our own credit risk in its assessment of fair value.

The following table presents our financial assets and liabilities that are carried at fair value, classified according to the three categories described above (in thousands):

	Fair Value Measurement at June 30, 2015			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Cash equivalents money market funds	$ 26,458	$ 26,458	$	$
Cash equivalents commercial paper	9,249		9,249	
Cash equivalents corporate bonds	4,319		4,319	
Total assets	$ 40,026	$ 26,458	$ 13,568	$
Liabilities:				
Contingent acquisition consideration	$ 4,997	$	$	$ 4,997
Total liabilities	$ 4,997	$	$	$ 4,997

	Fair Value Measurement at December 31, 2014			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Cash equivalents money market funds	$ 34,309	$ 34,309	$	$
Cash equivalents commercial paper	3,000		3,000	
Cash equivalents U.S. government and agency securities	2,700		2,700	
Total assets	$ 40,009	$ 34,309	$ 5,700	$
Liabilities:				
Contingent acquisition consideration	$ 270	$	$ 270	$
Total liabilities	$ 270	$	$ 270	$

The Company s recurring fair value measures relate to short-term investments, which are classified as cash equivalents, derivative instruments and contingent consideration. The fair value of our cash equivalents are either based on quoted prices for similar assets or other observable inputs such as yield curves at commonly quoted intervals and other market corroborated inputs. The fair value of our derivative instruments is based on quoted market prices from various banking institutions or an independent third party provider for similar instruments. In determining the fair value, we consider our non-performance risk and that of our counterparties. At June 30, 2015, we had one 30-day forward contract to sell 2.2 million British pound sterling and purchase $3.4 million that together, had an immaterial fair value. At December 31, 2014, we had one 30-day forward contract to sell 2.3 million British pound sterling and purchase $3.5 million that together, had an immaterial fair value.

For the contingent acquisition consideration classified as Level 2 at December 31, 2014, fair value approximated book value, and represented the amount to be paid based on actual achievement of the criteria.

At June 30, 2015, the Company had recorded approximately $5.0 million in contingent consideration related to the January 2015 acquisition of Swyft Media. The contingent consideration is payable in cash based on the achievement of certain revenue and EBITDA margin targets for the years ending December 31, 2015 through 2016, with a catch-up period for the year ending December 31, 2017, and subject to a cap of $15.0 million. The fair value of this liability was estimated using a Monte Carlo simulation model, relying on significant inputs that are not observable in the market and thus represent a Level 3 fair value measurement. The significant inputs in the Level 3 measurement not supported by market activity included our expected revenues and

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EBITDA for each of the measurement periods and the estimated level of risk and volatility around the forecast. The Monte Carlo simulation was relied on to estimate the projected revenues, EBITDA margins, and contingent acquisition consideration payments for each measurement period. The average contingent acquisition consideration payments for the years 2015 through 2017, following 100,000 simulation trials, were discounted to present value to capture the time value of money and counterparty risk, based upon an assessment of the Company s borrowing risk, and applying its credit rating to adjust the risk free rate.

The changes in the estimated fair value for our liabilities measured on a recurring basis using significant unobservable inputs (Level 3) are as follows (in thousands):

	Three Months Ended June 30, 2015	Six Months Ended June 30, 2015
Fair value measurement at the beginning of period	$ 4,900	$
Contingent consideration recorded upon acquisition		4,900
Accreted interest	97	97
Fair value measurement at end of period	$ 4,997	$ 4,997

The Company s non-financial assets and non-financial liabilities subject to non-recurring measurements include goodwill and intangible assets.

7. Property and Equipment

Property and equipment consists of the following (in thousands):

	June 30, 2015	December 31, 2014
Computer equipment and software	$ 17,472	$ 12,084
Furniture and fixtures	1,122	1,093
Leasehold improvements	3,957	3,498
Total cost	22,551	16,675
Less accumulated depreciation and amortization	(6,940)	(6,097)
Property and equipment, net	$ 15,611	$ 10,578

8. Intangible Assets

Intangible assets consist of the following (dollar amounts in thousands):

		June 30, 2015			December 31, 2014		
	Weighted-Average Amortization Period (Years)	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Balance**	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Balance**
Customer relationships	10	$ 60,175	$ (47,818)	$ 12,357	$ 57,488	$ (47,018)	$ 10,470
Acquired technology	11	54,604	(36,860)	17,744	55,064	(34,411)	20,653
Non-compete agreements	4	12,979	(11,948)	1,031	12,172	(11,862)	310
Indefinite-lived intangible assets:							
Trademarks		38,024		38,024	38,029		38,029
Domain names		4,400		4,400	4,400		4,400
Total		$ 170,182	$ (96,626)	$ 73,556	$ 167,153	$ (93,291)	$ 73,862

9. Debt

On July 13, 2011, the Company entered into a credit agreement (Credit Facility), with Wells Fargo Capital Finance, LLC, the administrative agent for a syndicate of Lenders (Lenders), which provides the Company with a five-year, $120.0 million secured revolving credit facility. Borrowings under the Credit Facility bear interest at a variable rate based upon, at the Company s option, either LIBOR or the base rate (which is the highest of (i) the prime rate, (ii) 0.5% plus the overnight federal funds rate, and (iii) 1.0% in excess of the three-month LIBOR rate), plus in each case, an applicable margin. The applicable margin for LIBOR loans, based on the applicable leverage ratio, is either 1.5% or 2.0% per annum, and the applicable margin for base rate loans, based on the applicable leverage ratio, is either 0.5% or 1.0% per annum. At June 30, 2015 our rate, inclusive of applicable margins, was 3.75% for prime. At June 30, 2015, the Company had no outstanding debt under the Credit Facility. The Company is required to pay an unused line fee equal to 0.375% per annum on the undrawn portion available under the revolving credit facility and variable per annum fees in respect of outstanding letters of credit, if any. Such fees are included in interest expense in the accompanying condensed consolidated statements of income.

The Credit Facility contains two financial covenants; a leverage ratio and a fixed charge coverage ratio. Failure to comply with these covenants, or the occurrence of an event of default, could permit the Lenders under the Credit Facility to declare all amounts borrowed under the Credit Facility, together with accrued interest and fees, to be immediately due and payable. In addition, the Credit Facility is secured by substantially all of our assets and places limits on the Company s and its subsidiaries ability to incur debt or liens and engage in sale-leaseback transactions, make loans and investments, incur additional indebtedness, engage in mergers, acquisitions and asset sales, transact with affiliates and alter its business. We were in compliance with all covenants under our Credit Facility as of June 30, 2015.

10. Defined Benefit Pension Plan

Our German subsidiary maintains an unfunded defined benefit pension plan which covers substantially all employees who joined the company prior to the plan s closure to new participants in 2006. Participants are entitled to benefits in the form of retirement, disability and surviving dependent pensions. Benefits generally depend on years of service and the salary of the employees.

The components of net periodic benefit cost included in the accompanying condensed consolidated statements of income were as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Service cost	$ 30	$ 29	$ 59	$ 59
Interest cost	30	44	58	88
Amortization	19		38	
Net periodic benefit cost	$ 79	$ 73	$ 155	$ 147

11. Income Taxes

A reconciliation of income taxes computed at federal statutory rates to income tax expense is as follows (dollar amounts in thousands):

	Three Months Ended June 30,			
	2015		2014	
Provision for income taxes at statutory rate	$ 3,180	35.0%	$ 4,284	35.0%
State and local income taxes, net of federal tax benefit	130	1.4%	225	1.8%
Stock compensation	30	0.3%	78	0.6%
Foreign rate differential	(99)	(1.1)%		
Disqualifying dispositions of incentive stock options	(3)		(25)	(0.2)%
Other, net	(55)	(0.6)%	(13)	
Reported income tax provision	$ 3,183	35.0%	$ 4,549	37.2%

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	Six Months Ended June 30,			
	2015		2014	
Provision for income taxes at statutory rate	$ 7,001	35.0%	$ 9,028	35.0%
State and local income taxes, net of federal tax benefit	287	1.4%	481	1.9%
Stock compensation	62	0.3%	165	0.6%
Reversal of reserves	(342)	(1.7)%		
Foreign rate differential	(186)	(0.9)%	178	0.7%
Disqualifying dispositions of incentive stock options	(19)	(0.1)%	(42)	(0.2)%
Other, net	(61)	(0.3)%	(153)	(0.6)%
Reported income tax provision	$ 6,742	33.7%	$ 9,657	37.4%

At June 30, 2015, the reserve for uncertain tax positions was approximately $6.5 million. Of this amount, $3.7 million is recorded as a reduction of deferred tax assets and $2.8 million is classified as long term liabilities. During the first quarter of 2015, the Company settled a tax audit related to its Japan subsidiary. As a result of this settlement, the Company recognized a tax benefit of $0.3 million.

12. Net Income Per Share

Basic and diluted earnings per share are computed pursuant to the two-class method. The two-class method determines earnings per share for each class of common stock and participating security according to their respective participation rights in undistributed earnings. Unvested restricted stock awards granted to employees are considered participating securities as they receive non-forfeitable rights to cash dividends at the same rate as common stock. In accordance with Accounting Standards Codification Topic No. 260, *Earnings Per Share*, diluted net income per share is calculated using the more dilutive of the following two approaches:

1. Assume exercise of stock options and vesting of restricted stock using the treasury stock method.

2. Assume exercise of stock options using the treasury stock method, but assume participating securities (unvested restricted stock) are not vested and allocate earnings to common shares and participating securities using the two-class method.

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For the three and six months ended June 30, 2015 and the three months ended June 30, 2014, the two-class method was used in the computation of diluted net income per share as this approach was more dilutive. For the six months ended June 30, 2014, the treasury stock method was used in the computation of diluted net income per share, as this approach was more dilutive. The following presents a reconciliation of the numerator and denominator used in the calculation of basic and diluted net income per share (in thousands, except share and per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Numerator:				
Net income, as reported	$ 5,904	$ 7,691	$ 13,261	$ 16,136
Less: net income attributable to participating securities	(150)	(159)	(301)	(289)
Net income available to common shareholders basic	$ 5,754	$ 7,532	$ 12,960	$ 15,847
Denominator:				
Basic:				
Weighted-average shares of common stock outstanding	39,873,730	39,555,875	39,758,947	39,438,705
Less: weighted-average shares of unvested restricted common stock outstanding	(1,047,545)	(841,697)	(931,279)	(725,273)
Weighted-average number of common shares used in computing basic net income per common share	38,826,185	38,714,178	38,827,668	38,713,432
Net income per share applicable to common shareholders basic	$ 0.15	$ 0.19	$ 0.33	$ 0.41

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Numerator:				
Net income available to common shareholders basic	$ 5,754	$ 7,532	$ 12,960	$ 15,847
Add-back: undistributed earnings allocated to unvested shareholders (1)	51	96	124	N/A
Less: undistributed earnings reallocated to unvested shareholders (1)	(50)	(94)	(122)	N/A

Net income available to common shareholders diluted	$	5,755	$	7,534	$	12,962	$	15,847

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	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Denominator:				
Diluted:				
Weighted-average shares of common stock outstanding	39,873,730	39,555,875	39,758,947	39,438,705
Less: weighted-average shares of unvested restricted common stock outstanding	(1,047,545)	(841,697)	(931,279)	(725,273)
Weighted-average number of common shares issuable upon exercise of outstanding stock options, based on the treasury stock method	569,210	909,339	631,090	973,470
Weighted-average number of restricted stock, based on the treasury stock method (2)	N/A	N/A	N/A	179,004
Weighted-average number of common shares used in computing diluted net income per common share	39,395,395	39,623,517	39,458,758	39,865,906
Net income per share applicable to common shareholders diluted	$ 0.15	$ 0.19	$ 0.33	$ 0.40

(1) Adjustments to net income relate to net income per share calculations under the two class method; therefore, it is not applicable, or N/A, for certain periods presented.

(2) Adjustments pertain to net income per share calculations under the treasury stock method; therefore, it is not applicable, or N/A, for certain periods presented.

The following common share equivalents have been excluded from the computation of diluted weighted-average shares outstanding, as their effect would have been anti-dilutive:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Options	433,463	689,410	370,201	417,058
Unvested restricted stock	405,522	395,520	247,768	233,813
Unvested restricted stock units	14,825	5,700	11,341	3,420

13. Stockholders Equity

Share repurchases

On October 23, 2013, the Company s Board of Directors approved a share repurchase program permitting repurchases of up to $50.0 million of the Company s outstanding shares of common shares for a maximum period of two years. Intended to offset shareholder dilution, the Company made repurchases periodically, on the open market as business and market conditions warrant through June 5, 2015, at which date the maximum amount of repurchases was reached. During the quarter ended June 30, 2015, the Company repurchased a total of 457,128 shares of its common stock for an aggregate purchase price of $12.5 million, including brokers fees. Of that amount, the Company purchased 14,278 shares of common stock, for an aggregate purchase price of $0.4 million, including brokers fees, in excess of its publicly announced share repurchase program upon the conclusion of the program.

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Share Based Compensation

We account for share based compensation in accordance with ASC Topic No. 718, *Compensation Stock Compensation,* which requires the measurement of compensation costs at fair value on the date of grant and recognition of compensation expense over the service period for awards expected to vest. The following presents the impact of share based compensation expense on our condensed consolidated statements of income (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Marketing and selling	$ 1,609	$ 1,250	$ 2,875	$ 2,296
Research and development	644	613	1,186	1,127
General and administrative	1,217	893	2,180	1,593
Total expensed	$ 3,470	$ 2,756	$ 6,241	$ 5,016
Property and equipment	40	40	82	63
Total share based compensation	$ 3,510	$ 2,796	$ 6,323	$ 5,079

In the three months ended June 30, 2015 and 2014, approximately $40 thousand and $40 thousand, respectively, and in the six months ended June 30, 2015 and 2014, approximately $82 thousand and $63 thousand, respectively, of share based compensation was capitalized as part of an internal software project, and this amount is included in property and equipment, net in our condensed consolidated balance sheet. As of June 30, 2015, the Company had $30.4 million of unrecognized compensation expense related to employees and directors unvested stock option awards, restricted stock units and restricted stock awards that are expected to be recognized over a weighted-average period of 2.9 years.

14. Segment Reporting

We view our operations and manage our business as one segment: the development, marketing and licensing of technologies and fonts. Factors used to identify our single segment include the financial information available for evaluation by our chief operating decision maker in making decisions about how to allocate resources and assess performance. While our technologies and services are sold into two principal markets, Creative Professional and OEM, expenses and assets are not formally allocated to these market segments, and operating results are assessed on an aggregate basis to make decisions about the allocation of resources. The following table presents revenue for these two major markets (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Creative Professional	$ 20,678	$ 18,266	$ 41,182	$ 35,985
OEM	25,727	26,697	51,269	55,050
Total	$ 46,405	$ 44,963	$ 92,451	$ 91,035

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Geographic segment information

The Company attributes revenue to geographic areas based on the location of our subsidiary receiving such revenue. For example, licenses may be sold to large international companies which may be headquartered in South Korea, but the sales are received and recorded by our subsidiary located in the United States. In this example, the revenue would be reflected in the United States totals in the table below. We market our products and services through offices in the United States, United Kingdom, Germany, Hong Kong, South Korea and Japan. The following summarizes revenue by location:

	Three Months Ended June 30,			
	2015		2014	
	Sales	% of Total	Sales	% of Total
	(In thousands, except percentages)			
United States	$ 26,520	57.2%	$ 24,602	54.7%
United Kingdom	1,530	3.3	2,636	5.9
Germany	5,389	11.6	4,210	9.4
Japan	12,773	27.5	13,367	29.7
Other Asia	193	0.4	148	0.3
Total	$ 46,405	100.0%	$ 44,963	100.0%

	Six Months Ended June 30,			
	2015		2014	
	Sales	% of Total	Sales	% of Total
	(In thousands, except percentages)			
United States	$ 51,363	55.5%	$ 48,538	53.3%
United Kingdom	3,378	3.7	5,329	5.9
Germany	11,233	12.2	8,687	9.5
Japan	25,980	28.1	28,081	30.9
Other Asia	497	0.5	400	0.4
Total	$ 92,451	100.0%	$ 91,035	100.0%

Long-lived assets, which include property and equipment, goodwill and intangible assets, but exclude other assets, long-term investments and deferred tax assets, are attributed to geographic areas in which Company assets reside and is shown below (in thousands):

	June 30, 2015	December 31, 2014
Long-lived assets:		
United States	$ 210,344	$ 189,927
United Kingdom	4,992	5,138

Germany	57,500	62,917
Asia (including Japan)	3,525	3,457
Total	$ 276,361	$ 261,439

15. Commitments and Contingencies

Legal Proceedings

From time to time, we may be a party to various claims, suits and complaints. We do not believe that there are claims or legal proceedings that, if determined adversely to us, would have a material adverse effect on our business, results of operations or financial condition.

Licensing Warranty

Under our standard license agreement with our OEM customers, we warrant that the licensed technologies are free of infringement claims of intellectual property rights and will meet the specifications as defined in the licensing agreement for a one year period. Under the licensing agreements, liability for such indemnity obligations is limited generally to the total arrangement fee; however, exceptions have been made on a case-by-case basis, increasing the maximum potential liability to agreed upon amounts at the time the contract is entered into or unlimited liability. We have never incurred costs payable to a customer or business partner to defend lawsuits or settle claims related to these warranties, and as a result, management believes the estimated fair value of these warranties is minimal. Accordingly, there are no liabilities recorded for these warranties as of June 30, 2015 and December 31, 2014.

16. Subsequent Event

Dividend Declaration

On July 22, 2015 the Company s Board of Directors declared a $0.10 per share quarterly cash dividend on our outstanding common stock. The record date is set for October 1, 2015 and the dividend is payable to shareholders of record on October 21, 2015. Dividends are declared at the discretion of the Company s Board of Directors and depend on actual cash from operations, the Company s financial condition and capital requirements and any other factors the Company s Board of Directors may consider relevant. Future dividend declarations, as well as the record and payment dates for such dividends, will be determined by the Company s Board of Directors on a quarterly basis.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Forward Looking Statements and Projections

This Quarterly Report on Form 10-Q contains forward looking statements. Forward looking statements relate to future events or our future financial performance. We generally identify forward looking statements by terminology such as may, will, should, expects, plans, anticipates, could, intends, target, projects, contemplates, believes, estimates, predicts, potential or continue or the negative of these terms or other similar words. These statements are only predictions. We have based these forward looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our business, results of operations and financial condition. The outcome of the events described in these forward looking statements is subject to risks, uncertainties and other factors described in Management s Discussion and Analysis of Financial Condition and Results of Operations, Risk Factors and elsewhere in this Quarterly Report on Form 10-Q. Accordingly, you should not rely upon forward looking statements as predictions of future events. We cannot assure you that the events and circumstances reflected in the forward looking statements will be achieved or occur, and actual results could differ materially from those projected in the forward looking statements. The forward looking statements made in this Quarterly Report on Form 10-Q relate only to events as of the date on which the statements are made. We undertake no obligation to update any forward looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events.

Overview

We are a leading provider of type, technology and expertise for creative applications and consumer devices. Our vision is that our fonts and technology empower every word and experience. We strive to enable the best user experience and ensure brand integrity, regardless of device, platform or language. We help creative professionals, consumer device manufacturers and independent software vendors connect their brands, content, products and services to consumers and businesses everywhere, from content creation to consumption. Monotype is home to some of the world s best known typeface collections. Along with our custom type services, our solutions enable customers to express their creativity, while our tools and technologies improve creative workflows and maximize efficiency as content is published or distributed. Our solutions provide worldwide language coverage and high-quality text, and our embedded solutions support compelling user interfaces and brand fidelity by providing for the display of content on any device or platform, as the author intended. We offer more than 25,000 typeface designs, and include some of the world s most widely used designs, such as the Times New Roman®, Helvetica®, Frutiger®, ITC Franklin Gothic , FF Meta and Droid typefaces, and support more than 250 Latin and non-Latin languages. Our e-commerce websites, including *myfonts.com, fonts.com, fontshop.com, linotype.com* and *fontfont.com,* which attracted more than 77 million visits in 2014 from over 200 countries and territories, offer thousands of high-quality font products, in some cases more than 127,000, including our own fonts from the Monotype Libraries as well as fonts from third parties.

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Sources of Revenue

We derive revenue from two principal sources: licensing our fonts and font related services to creative and business professionals, which we refer to as our Creative Professional revenue, and licensing our text imaging solutions to consumer device manufacturers and independent software vendors, which we refer to as our OEM revenue. We derive our Creative Professional revenue primarily from brands, agencies, publishers, corporations, enterprises, small businesses and individuals. Some of our revenue streams, particularly custom revenue where spending is largely discretionary in nature, have historically been and we expect them to continue to be in the future, susceptible to weakening economic conditions.

Geographic revenue, which is based on the location of our subsidiary receiving such revenue, is in the table below:

	Three Months Ended June 30,			
	2015		2014	
	Sales	% of Total	Sales	% of Total
	(In thousands, except percentages)			
United States	$ 26,520	57.2%	$ 24,602	54.7%
United Kingdom	1,530	3.3	2,636	5.9
Germany	5,389	11.6	4,210	9.4
Japan	12,773	27.5	13,367	29.7
Other Asia	193	0.4	148	0.3
Total	$ 46,405	100.0%	$ 44,963	100.0%

	Six Months Ended June 30,			
	2015		2014	
	Sales	% of Total	Sales	% of Total
	(In thousands, except percentages)			
United States	$ 51,363	55.5%	$ 48,538	53.3%
United Kingdom	3,378	3.7	5,329	5.9
Germany	11,233	12.2	8,687	9.5
Japan	25,980	28.1	28,081	30.9
Other Asia	497	0.5	400	0.4
Total	$ 92,451	100.0%	$ 91,035	100.0%

For the three months ended June 30, 2015 and 2014, sales by our subsidiaries located outside the United States comprised 42.8% and 45.3%, respectively, of our total revenue. For the six months ended June 30, 2015 and 2014, sales by our subsidiaries located outside the United States comprised 44.5% and 46.7%, respectively, of our total revenue. We expect that sales by our international subsidiaries will continue to represent a substantial portion of our revenue for the foreseeable future. Future international revenue will depend on the continued use and expansion of our text imaging solutions worldwide.

We derive a significant portion of our OEM revenue from a limited number of customers, in particular manufacturers of laser printers and consumer electronics. For the three months ended June 30, 2015 and 2014, our top ten licensees by revenue, all of which are with OEM customers, accounted for approximately 34.1% and 36.1% of our total revenue, respectively. For the six months ended June 30, 2015 and 2014, our top ten licensees by revenue, all of which are with OEM customers, accounted for approximately 34.8% and 37.4% of our total revenue, respectively. As Creative Professional revenue growth is expected to continue to outpace OEM revenue growth, we expect total revenue from our top ten licensees to continue to decrease as a percentage of total revenue. Although no one customer accounted for 10% or moreof our total revenue for the three or six months ended June 30, 2015 or 2014, if we are unable to maintain relationships with major customers or establish relationships with new customers, our licensing revenue will be adversely affected.

Creative Professional Revenue

Our Creative Professional revenue is derived from font licenses, font related services and from custom font design services. We license fonts directly to end-users through our e-commerce websites, via telephone, email and indirectly through third-party resellers. Font related services refer to our web font services and web design tools. We also license fonts and provide custom font design services to graphic designers, advertising agencies, media organizations and corporations. We refer to direct, indirect and custom revenue, as non-web revenue, and refer to revenue that is derived from our websites, as web revenue.

Revenue from font licenses to our e-commerce customers is recognized upon payment by the customer and the software embodying the font is shipped or made available. Revenue from font licenses to other customers is recognized upon shipment of the software embodying the font and when all other revenue recognition criteria have been met. Revenue from resellers is recognized upon notification from the reseller that our font product has been licensed and when all other revenue recognition criteria have been met. Custom font design services revenue is generally recognized upon delivery, unless it is part of a bundled services arrangement, in which case, it is recognized over the longest service period. Font related service revenue is mainly subscription based and it may contain software as a service. The subscription revenue is recognized ratably over the subscription period. We consider web server and commercial rights to online fonts as recurring revenue and it is recognized upon invoicing and proof of font delivery, when all other revenue recognition criteria have been met. Contract accounting is used where services are deemed essential to the software. We consider both the completed contract and percentage-of-completion method of revenue recognition for contract accounting arrangements. We have the ability to make reasonable estimates, and therefore, typically use the percentage-of-completion method in arrangements subject to contract accounting applying input or output measures, where appropriate. We make certain judgements, by estimating the amount of expenses to be recognized, together with the percent of revenue earned in each particular period.

OEM Revenue

Our OEM revenue is derived substantially from per-unit royalties received for printer imaging and printer driver, or printer products, and display imaging products. Under our licensing arrangements we typically receive a royalty for each product unit incorporating our text imaging solutions that is shipped by our OEM customers. We also receive OEM revenue from fixed fee licenses with certain of our OEM customers. Fixed fee licensing arrangements are not based on units the customer ships, but instead, customers pay us on a periodic basis for the right to embed our typefaces and technology. Although significantly less than royalties from per-unit shipments and fixed fees from OEM customers, we also receive revenue from software application and operating systems vendors, who include our typefaces and technology in their products, and for font development. Many of our per-unit royalty licenses continue for the duration that our OEM customers ship products that include our technology, unless terminated for breach. Other licenses have terms that typically range from one to five years, and usually provide for automatic or optional renewals. We recognize revenue from per-unit royalties in the period during which we receive a royalty report from a customer, typically one quarter after royalty-bearing units are shipped, as we do not have the ability to estimate the number of units shipped by our customers. Revenue from fixed fee licenses is generally recognized when it is billed to the customer, so long as the product has been delivered, the license fee is fixed and non-refundable and collection is probable. OEM revenue also includes project-related agreements for which contract accounting may be used.

Cost of Revenue

Our cost of revenue consists of font license fees that we pay on certain fonts that are owned by third parties, allocated internal engineering expense and overhead costs directly related to custom design services. License fees that we pay to third parties are typically based on a percentage of our Creative Professional and OEM revenue and do not involve minimum fees. Our cost of OEM revenue is typically lower than our cost of Creative Professional revenue because we own a higher percentage of the fonts licensed to our OEM customers, provide value-added technology and have negotiated lower royalty rates on the fonts we license from third parties because of volume. The cost of our custom design service revenue is substantially higher than the cost of our other revenue and, as a result, our gross margin varies from period-to-period depending on the level of custom design revenue recorded.

Cost of revenue also includes amortization of acquired technology, which we amortize over 8 to 15 years. For purposes of amortizing acquired technology we estimate the remaining useful life of the technology based upon various considerations, including our knowledge of the technology and the way our customers use it. We use the straight-line method to amortize our acquired technology as there is no reliable evidence to suggest that we should expect any other pattern of amortization than an even pattern, and we believe this best reflects the expected pattern of economic usage.

Gross Profit

Our gross profit percentage is influenced by a number of factors including product mix, pricing and volume at any particular time. However, our cost of OEM revenue is typically lower than our cost of Creative Professional revenue because we own a higher percentage of the fonts licensed to our OEM customers, provide value-added technology and have negotiated lower royalty rates on the fonts we license from third parties because of volume. Within our Creative Professional business, the cost of our custom design service revenue is substantially higher than the cost of our other revenue. As a result, our gross profit varies from period-to-period depending on the mix between, and within, Creative Professional and OEM revenue.

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Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with GAAP and our discussion and analysis of our financial condition and results of operations requires us to make judgments, assumptions and estimates that affect the amounts reported in our consolidated financial statements and accompanying notes. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for judgments about the carrying values of assets and liabilities. Actual results may differ from these estimates.

There has been no material change in our critical accounting policies since December 31, 2014. Information about our critical accounting policies may be found in Part II, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, under the heading Critical Accounting Policies, of our Annual Report on Form 10-K for the year ended December 31, 2014.

Results of Operations for the Three Months Ended June 30, 2015 Compared to Three Months Ended June 30, 2014

The following table sets forth items in the condensed consolidated quarterly statements of income as a percentage of sales for the periods indicated:

	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014
Revenue:		
Creative Professional	44.6%	40.6%
OEM	55.4	59.4
Total revenue	100.0	100.0
Cost of revenue	16.3	16.3
Cost of revenue amortization of acquired technology	2.4	2.5
Total cost of revenue	18.7	18.8
Gross profit	81.3	81.2
Marketing and selling	31.3	26.7
Research and development	11.4	10.9
General and administrative	15.1	12.0
Amortization of other intangible assets	1.7	3.2
Total operating expenses	59.5	52.8
Income from operations	21.8	28.4
Interest expense, net	0.7	0.6
Loss on foreign exchange	1.1	0.3
Loss on derivatives	0.4	0.3
Other income, net		

Total other expense	2.2	1.2
Income before provision for income taxes	19.6	27.2
Provision for income taxes	6.9	10.1
Net income	12.7%	17.1%

The following discussion compares the three months ended June 30, 2015 with the three months ended June 30, 2014.

Revenue by Market.

We view our operations and manage our business as one segment: the development, marketing and licensing of technologies and fonts. Factors used to identify our single segment include the financial information available for evaluation by our chief operating decision maker in making decisions about how to allocate resources and assess performance. While our technologies and services are sold to customers in two principal markets, Creative Professional and consumer device manufacturers and independent software vendors, together OEM, expenses and assets are not formally allocated to these markets, and operating results are assessed on an aggregate basis to make decisions about the allocation of resources.

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The following table presents revenue for these two principal markets (in thousands):

	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014	Increase/ (Decrease)
Creative Professional	$ 20,678	$ 18,266	$ 2,412
OEM	25,727	26,697	(970)
Total revenue	$ 46,405	$ 44,963	$ 1,442

Revenue

Revenue was $46.4 million and $45.0 million for the three months ended June 30, 2015 and 2014, respectively, an increase of $1.4 million, or 3.2%.

Creative Professional revenue increased $2.4 million, or 13.2%, to $20.7 million for the three months ended June 30, 2015, as compared to $18.3 million for the three months ended June 30, 2014, mainly from increased web revenue due to increased font license revenue and increased sales of our web font services.

OEM revenue was $25.7 million and $26.7 million for the three months ended June 30, 2015 and 2014, respectively, a decrease of $1.0 million, or 3.6%. Decreased revenue from per unit royalty arrangements with our printer and display imaging consumer electronic OEM customers was partially offset by increased revenue from our independent software vendor customers, mainly due to the timing of certain non-recurring license deals in the second quarter of 2014.

Cost of Revenue and Gross Profit

Cost of revenue, excluding amortization of acquired technology, was $7.6 million and $7.3 million for the three months ended June 30, 2015 and 2014, respectively, an increase of $0.3 million, or 3.2%. As a percentage of total revenue, cost of revenue, excluding amortization of acquired technology, was consistent at 16.3% in the three months ended June 30, 2015 and 2014, respectively. In the second quarter of 2015, as compared to the same period in 2014, custom font design revenue had a lower associated cost, the impact of which was offset by an increase in Creative Professional revenue, which typically has a higher associated cost than our OEM revenue. In the three months ended June 30, 2015, Creative Professional revenue was 44.6% of total revenue, as compared to 40.6% of total revenue in the same period in 2014.

The portion of cost of revenue consisting of amortization of acquired technology was unchanged at $1.1 million for the three months ended June 30, 2015 and 2014, respectively.

Gross profit in the three months ended June 30, 2015 and 2014 was consistent at 81.3% and 81.2% of sales, respectively. In the second quarter of 2015, as compared to the same period in 2014, we achieved improved gross profit on custom font development revenue, which was offset by a higher mix of Creative Professional revenue, as detailed above.

Operating Expenses

Marketing and Selling. Marketing and selling expense increased $2.5 million, or 21.2%, to $14.5 million in the three months ended June 30, 2015, as compared to $12.0 million in the three months ended June 30, 2014. Personnel expenses increased $1.9 million due to additional headcount primarily from our acquisitions of Swyft Media and FontShop, and increased share based compensation in the three months ended June 30, 2015, as compared to the same period in 2014. Increased infrastructure expenses, primarily rent and depreciation expense, mainly associated with our new corporate office, contributed $0.5 million to the increase in the three months ended June 30, 2015, as compared to the same period in 2014.

Research and Development. Research and development expense was $5.3 million in the three months ended June 30, 2015, as compared to $4.9 million in the three months ended June 30, 2014, an increase of $0.4 million, or 7.7%, primarily from an increase in personnel and consulting expenses.

General and Administrative. General and adm