

LogMeIn, Inc.  
Form 10-Q  
April 28, 2011

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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 March 31, 2011**

**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: 001-34391**

**LOGMEIN, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

**20-1515952**

(State or other jurisdiction of incorporation or  
organization)

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

**500 Unicorn Park Drive  
Woburn, Massachusetts**

**01801**

(Address of principal executive offices)

(Zip Code)

**781-638-9050**

(Registrant's telephone number, including area code)

(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  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. (Check one):

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

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

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As of April 22, 2011, there were 24,052,007 shares of the registrant's Common Stock, par value \$.01 per share, outstanding.

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**LogMeIn, Inc.**  
**Condensed Consolidated Balance Sheets**

	<b>December 31, 2010</b>	<b>March 31, 2011</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 77,279,987	\$ 86,081,727
Marketable securities	90,144,484	90,133,823
Accounts receivable (net of allowance for doubtful accounts of \$111,000 as of December 31, 2010 and March 31, 2011)	4,744,392	5,873,614
Prepaid expenses and other current assets (including \$9,000 and \$0 of non-trade receivable due from related party at December 31, 2010 and March 31, 2011, respectively)	2,905,618	2,440,586
Deferred income tax assets	1,315,529	1,326,923
Total current assets	176,390,010	185,856,673
Property and equipment, net	6,198,487	6,448,220
Restricted cash	350,481	389,201
Intangibles, net	577,815	532,188
Goodwill	615,299	615,299
Other assets	27,019	62,219
Deferred income tax assets	2,518,158	2,519,356
Total assets	\$ 186,677,269	\$ 196,423,156
 <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 2,176,390	\$ 4,849,366
Accrued liabilities	10,829,310	9,812,013
Deferred revenue, current portion	41,763,138	46,177,082
Total current liabilities	54,768,838	60,838,461
Deferred revenue, net of current portion	1,030,017	1,390,037
Other long-term liabilities	500,156	459,669
Total liabilities	56,299,011	62,688,167
 Commitments and contingencies (Note 8)		
Preferred stock, \$0.01 par value 5,000,000 shares authorized, 0 shares outstanding as of December 31, 2010 and March 31, 2011		
Stockholders equity:		
Common stock, \$0.01 par value 75,000,000 shares authorized as of December 31, 2010 and March 31, 2011; 23,858,514 and 24,021,282 shares outstanding as of December 31, 2010 and March 31, 2011, respectively	238,585	240,213
Additional paid-in capital	133,425,098	136,290,131
Accumulated deficit	(3,084,316)	(3,149,563)

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Accumulated other comprehensive income (loss)	(201,109)	354,208
Total stockholders' equity	130,378,258	133,734,989
Total liabilities and stockholders' equity	\$ 186,677,269	\$ 196,423,156

See notes to condensed consolidated financial statements.

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**LogMeIn, Inc.**  
**Condensed Consolidated Statements of Operations**

	<b>Three Months Ended March 31,</b>	
	<b>2010</b>	<b>2011</b>
Revenue (including \$1,487,000 and \$0 from a related party during the three months ended March 31, 2010 and 2011, respectively)	\$ 21,324,800	\$ 27,038,779
Cost of revenue	2,220,163	2,536,136
Gross profit	19,104,637	24,502,643
Operating expenses		
Research and development	3,553,797	4,317,779
Sales and marketing	9,840,481	12,986,109
General and administrative	2,803,357	6,058,690
Legal settlements		1,250,000
Amortization of acquired intangibles	81,929	92,034
Total operating expenses	16,279,564	24,704,612
Income (loss) from operations	2,825,073	(201,969)
Interest income, net	114,142	210,712
Other expense	(64,037)	(108,811)
Income (loss) before income taxes	2,875,178	(100,068)
(Provision) benefit for income taxes	(139,159)	34,821
Net income (loss)	\$ 2,736,019	\$ (65,247)
Net income (loss) per share:		
Basic	\$ 0.12	\$ 0.00
Diluted	\$ 0.11	\$ 0.00
Weighted average shares outstanding:		
Basic	22,643,963	23,928,310
Diluted	24,350,845	23,928,310

See notes to condensed consolidated financial statements.

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**LogMeIn, Inc.**  
**Condensed Consolidated Statements of Cash Flows**

	<b>Three Months Ended March 31,</b>	
	<b>2010</b>	<b>2011</b>
<b>Cash flows from operating activities</b>		
Net income (loss)	\$ 2,736,019	\$ (65,247)
Adjustments to reconcile net income (loss) to net cash provided by operating activities		
Depreciation and amortization	941,530	1,004,987
Amortization of premium on investments	33,913	59,105
Provision for bad debts	30,000	14,050
Provision for deferred income taxes	4,000	(12,461)
Stock-based compensation	1,026,799	1,745,494
Gain on disposal of equipment	(1,238)	(178)
Changes in assets and liabilities:		
Accounts receivable	780,568	(1,143,272)
Prepaid expenses and other current assets	204,340	465,032
Other assets	(27,901)	(35,200)
Accounts payable	281,745	2,634,892
Accrued liabilities	(842,522)	(1,006,483)
Deferred revenue	2,265,579	4,773,964
Other long-term liabilities	(50,371)	(40,487)
Net cash provided by operating activities	7,382,461	8,394,196
<b>Cash flows from investing activities</b>		
Purchases of marketable securities	(55,331,450)	(30,076,850)
Proceeds from sale or disposal of marketable securities	25,000,000	30,000,000
Purchases of property and equipment	(365,001)	(1,117,622)
Intangible asset additions		(61,738)
Increase in restricted cash and deposits		(25,569)
Net cash used in investing activities	(30,696,451)	(1,281,779)
<b>Cash flows from financing activities</b>		
Payments of issuance costs related to secondary offering of common stock	(210,394)	
Proceeds from issuance of common stock upon option exercises	1,350,413	1,117,686
Net cash provided by financing activities	1,140,019	1,117,686
Effect of exchange rate changes on cash and cash equivalents and restricted cash	(133,907)	571,637
Net increase (decrease) in cash and cash equivalents	(22,307,878)	8,801,740
Cash and cash equivalents, beginning of period	100,290,001	77,279,987
Cash and cash equivalents, end of period	\$ 77,982,123	\$ 86,081,727



**Supplemental disclosure of cash flow information**

Cash paid for interest	\$	228	\$	118
Cash paid for income taxes	\$	16,626	\$	23,736

**Noncash investing and financing activities**

Purchases of property and equipment included in accounts payable and accrued liabilities	\$	817,709	\$	418,055
Deferred stock offering costs included in accounts payable and accrued liabilities	\$	18,493	\$	

See notes to condensed consolidated financial statements.

**Table of Contents****LogMeIn, Inc.****Notes to Condensed Consolidated Financial Statements****1. Nature of the Business**

LogMeIn, Inc. (the Company) develops and markets a suite of remote access, remote support, and collaboration solutions that provide instant, secure connections between Internet enabled devices. The Company's product line includes Gravity™, LogMeIn Free®, LogMeIn Pro<sup>2</sup>®, LogMeIn® Central™, LogMeIn Rescue®, LogMeIn® Rescue+Mobile™, LogMeIn Backup®, LogMeIn® Ignition SM™, LogMeIn Hamachi<sup>2</sup>®, join.me™ and RemotelyAnywhere®. The Company is based in Woburn, Massachusetts with wholly-owned subsidiaries in Hungary, The Netherlands, Australia, England and Brazil.

**2. Summary of Significant Accounting Policies**

*Principles of Consolidation* The accompanying condensed consolidated financial statements include the results of operations of the Company and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation. The Company has prepared the accompanying consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP).

*Unaudited Interim Condensed Consolidated Financial Statements* The accompanying condensed consolidated financial statements and the related interim information contained within the notes to the condensed consolidated financial statements are unaudited and have been prepared in accordance with GAAP and applicable rules and regulations of the Securities and Exchange Commission for interim financial information. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. The accompanying unaudited condensed consolidated financial statements should be read along with the Company's audited financial statements included in the Company's Annual Report on Form 10-K, filed with the Securities and Exchange Commission on February 28, 2011. The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and in the opinion of management, reflect all adjustments, consisting of normal and recurring adjustments, necessary for the fair presentation of the Company's financial position, results of operations and cash flows for the interim periods presented. The results for the interim periods presented are not necessarily indicative of future results. The Company considers events or transactions that occur after the balance sheet date but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure.

*Use of Estimates* The preparation of condensed consolidated 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 revenue and expenses during the reporting period. By their nature, estimates are subject to an inherent degree of uncertainty. Actual results could differ from those estimates.

*Marketable Securities* The Company's marketable securities are classified as available-for-sale and are carried at fair value with the unrealized gains and losses, net of tax, reported as a component of accumulated other comprehensive income in stockholders' equity. Realized gains and losses and declines in value judged to be other than temporary are included as a component of earnings based on the specific identification method. Fair value is determined based on quoted market prices. At December 31, 2010 and March 31, 2011, marketable securities consisted of U.S. government agency securities that have remaining maturities within two years and have an aggregate amortized cost of \$90,119,605 and \$90,137,350 and an aggregate fair value of \$90,144,484 and \$90,133,823, including \$65,136 and \$52,183 of unrealized gains and \$40,257 and \$55,711 of unrealized losses, respectively.

*Revenue Recognition* The Company derives revenue primarily from subscription fees related to its LogMeIn premium services and from the licensing of its Ignition for iPhone, iPad and Android software products and RemotelyAnywhere software and related maintenance.

Revenue from the Company's LogMeIn premium services is recognized on a daily basis over the subscription term as the services are delivered, provided that there is persuasive evidence of an arrangement, the fee is fixed or determinable and collectability is deemed reasonably assured. Subscription periods range from monthly to four years, but are generally one year in duration. The Company's software cannot be run on another entity's hardware nor do customers have the right to take possession of the software and use it on their own or another entity's hardware.

The Company recognizes revenue from the bundled delivery of its RemotelyAnywhere software product and related maintenance ratably, on a daily basis, over the term of the maintenance contract, generally one year, when there is persuasive evidence of an arrangement, the product has been provided to the customer, the collection of the fee is probable, and the amount of fees to be paid by the customer is fixed or determinable. The Company currently does not have vendor-specific objective evidence for the fair value of its maintenance arrangements and therefore the license and maintenance are bundled together. The Company recognizes revenue from the sale of its Ignition for iPhone, iPad and Android software product which is sold as a perpetual license and is recognized when there is persuasive evidence of an arrangement, the product has been provided to the customer, the collection of the fee is probable, and the amount of fees to be paid by the customer is fixed or determinable.

The Company's multi-element arrangements typically include multiple deliverables by the Company such as subscription and professional services, including development services. Agreements with multiple element deliverables are analyzed to determine if fair value

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exists for each element on a stand-alone basis. If the fair value of each deliverable is determinable using objective evidence or best estimate selling price, then revenue is recognized separately when or as the services are delivered, or if applicable, when milestones associated with the deliverable are achieved and accepted by the customer. If the fair value of any of the undelivered performance obligations cannot be determined, the arrangement is accounted for as a single element and the Company recognizes revenue on a straightline basis over the period in which the Company expects to complete its performance obligations under the agreement.

*Concentrations of Credit Risk and Significant Customers* The Company's principal credit risk relates to its cash, cash equivalents, marketable securities, restricted cash, and accounts receivable. Cash, cash equivalents, and restricted cash are deposited primarily with financial institutions that management believes to be of high-credit quality and custody of its marketable securities is with an accredited financial institution. To manage accounts receivable credit risk, the Company regularly evaluates the creditworthiness of its customers and maintains allowances for potential credit losses. To date, losses resulting from uncollected receivables have not exceeded management's expectations.

As of March 31, 2011, one customer accounted for 17% of accounts receivable, and no customers accounted for more than 10% of revenue for the three months ended March 31, 2010 or 2011. At December 30, 2010, there was one customer that accounted for 14% of accounts receivable.

*Foreign Currency Translation* The functional currency of operations outside the United States of America is deemed to be the currency of the local country. Accordingly, the assets and liabilities of the Company's foreign subsidiaries are translated into United States dollars using the period-end exchange rate, and income and expense items are translated using the average exchange rate during the period. Cumulative translation adjustments are reflected as a separate component of stockholders' equity. Foreign currency transaction gains and losses are charged to operations. The Company had foreign currency losses of approximately \$64,000 and \$109,000 for the three months ended March 31, 2010 and 2011, respectively.

*Stock-Based Compensation* Stock-based compensation is measured based upon the grant date fair value and recognized as an expense on a straight-line basis in the financial statements over the vesting period of the award for those awards expected to vest. The Company uses the Black-Scholes option pricing model to estimate the grant date fair value of stock awards. The Company uses the with-or-without method to determine when it will realize excess tax benefits from stock based compensation. Under this method, the Company will realize these excess tax benefits only after it realizes the tax benefits of net operating losses from operations.

*Income Taxes* Deferred income taxes are provided for the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, and operating loss carry-forwards and credits using enacted tax rates expected to be in effect in the years in which the differences are expected to reverse. At each balance sheet date, the Company assesses the likelihood that deferred tax assets will be realized, and recognizes a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction. As of December 31, 2010 and March 31, 2011, the Company maintained a full valuation allowance related to the deferred tax assets of its Hungarian subsidiary due to its historical net losses.

The Company evaluates its uncertain tax positions based on a determination of whether and how much of a tax benefit taken by the Company in its tax filings or positions is more likely than not to be realized. Potential interest and penalties associated with any uncertain tax positions are recorded as a component of income tax expense. Through March 31, 2011, the Company has not identified any material uncertain tax positions for which liabilities would be required.

*Comprehensive Income* Comprehensive income is the change in stockholders' equity during a period relating to transactions and other events and circumstances from non-owner sources and currently consists of net income (loss), foreign currency translation adjustments and unrealized gains and losses on available-for-sale securities. Comprehensive income was calculated as follows:

<b>Three Months Ended March</b>	
<b>31,</b>	
<b>2010</b>	<b>2011</b>

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Net income (loss)	\$ 2,736,019	\$ (65,247)
Cumulative translation adjustments	(143,593)	572,460
Unrealized gain on available-for-sale securities	(14,420)	(17,143)
Comprehensive income	\$ 2,578,006	\$ 490,070

*Net Income (Loss) Per Share* Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted net income (loss) per share is computed by dividing net income (loss) by the sum of the weighted average number of common shares outstanding during the period and the options to purchase common shares from the assumed exercise of stock options. For the three months ended March 31, 2011, the Company incurred a net loss and therefore, the effect of the Company's outstanding common stock equivalents were not included in the calculation of diluted loss per share as they were anti-dilutive. Accordingly, basic and diluted net loss per share for the period were identical.

The Company excluded 809,575 and 2,939,422 of options to purchase common shares from the computation of diluted net income (loss) per share for the three months ended March 31, 2010 and 2011, respectively, either because they had an anti-dilutive impact or because the Company had a net loss in the period.

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Basic and diluted net income (loss) per share was calculated as follows:

	<b>Three Months Ended March 31, 2010</b>
Basic:	
Net income	\$ 2,736,019
Weighted average common shares outstanding, basic	22,643,963
Net income, basic	\$ 0.12
Diluted:	
Net income	\$ 2,736,019
Weighted average common shares outstanding	22,643,963
Add: Options to purchase common shares	1,706,882
Weighted average common shares outstanding, diluted	24,350,845
Net income, diluted	\$ 0.11
	<b>Three Months Ended March 31, 2011</b>
Basic and diluted net loss per share:	
Net loss	\$ (65,247)
Weighted average common shares outstanding	23,928,310
Basic and diluted net loss per share	\$ 0.00

*Recently Issued Accounting Pronouncements* In October 2009, an update was made to *Revenue Recognition Multiple Deliverable Revenue Arrangements*. This update removes the objective-and-reliable-evidence-of-fair-value criterion from the separation criteria used to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting, replaces references to fair value with selling price to distinguish from the fair value measurements required under the *Fair Value Measurements and Disclosures* guidance, provides a hierarchy that entities must use to estimate the selling price, eliminates the use of the residual method for allocation, and expands the ongoing disclosure requirements. The effect of adoption of this standard has only impacted our financial statement disclosure to comply with the additional disclosure requirements as described in Note 2 to the condensed consolidated financial statements. The implementation of this guidance did not have a material impact on our consolidated financial position, results of operations or cash flows.

**3. Fair Value of Financial Instruments**

The carrying value of the Company's financial instruments, including cash equivalents, restricted cash, accounts receivable, and accounts payable, approximate their fair values due to their short maturities. The Company's financial assets and liabilities are measured using



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inputs from the three levels of the fair value hierarchy. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement. The three levels are as follows:

Level 1: Unadjusted quoted prices for identical assets or liabilities in active markets accessible by the Company at the measurement date.

Level 2: Inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3: Unobservable inputs that reflect the Company's assumptions about the assumptions that market participants would use in pricing the asset or liability.

The following table summarizes the basis used to measure certain of the Company's financial assets that are carried at fair value:

		<b>Basis of Fair Value Measurements</b>		
		<b>Quoted Prices in Active Markets for Identical Items (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
	<b>Balance</b>			
<b>Balance at December 31, 2010</b>				
Cash equivalents – money market funds	\$48,074,441	\$48,074,441	\$	\$
Cash equivalents – bank deposits	5,022,089		5,022,089	
Short-term marketable securities – U.S. government agency securities	90,144,484	90,144,484		
<b>Balance at March 31, 2011</b>				
Cash equivalents – money market funds	\$48,293,829	\$48,293,829	\$	\$
Cash equivalents – bank deposits	5,025,591		5,025,591	
Short-term marketable securities – U.S. government agency securities	90,133,823	90,133,823		

Bank deposits are classified within the second level of the fair value hierarchy and the fair value of those assets are determined based upon quoted prices for similar assets in active markets.

**4. Intangible Assets**

Acquired intangible assets consist of the following:

	<b>December 31, 2010</b>				<b>March 31, 2011</b>		
	<b>Estimated Useful Life</b>	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>	<b>Net Carrying Amount</b>	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>	<b>Net Carrying Amount</b>
Identifiable intangible assets:							
Trademark	5 years	\$ 635,506	\$ 563,105	\$ 72,401	\$ 635,506	\$ 594,880	\$ 40,626
Customer base	5 years	1,003,068	888,791	114,277	1,003,068	938,944	64,124
Domain names		202,120	10,038	192,082	202,107	20,143	181,964



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	5						
	years						
Software	4	298,977	298,977		298,977	298,977	
	years						
Technology	4	1,361,900	1,361,900		1,361,900	1,361,900	
Internally	years						
developed	3						
software	years	213,942	14,887	199,055	275,693	30,219	245,474
		\$ 3,715,513	\$ 3,137,698	\$ 577,815	\$ 3,777,251	\$ 3,245,063	\$ 532,188

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The Company capitalized \$61,751 of costs related to internally developed computer software to be sold as a service incurred during the application development stage during the three months ended March 31, 2011 and is amortizing these costs over the expected lives of the related services. No amounts were capitalized during the three months ended March 31, 2010 as the costs incurred during the period were immaterial.

The Company is amortizing the intangible assets on a straight-line basis over the estimated useful lives noted above. Amortization expense for intangible assets was \$185,733 and \$107,365 for the three months ended March 31, 2010 and 2011, respectively. Amortization relating to software, technology and internally developed software is recorded within cost of revenues and the amortization of trademark, customer base, and domain names is recorded within operating expenses. Future estimated amortization expense for intangible assets is as follows at March 31, 2011:

<b>Amortization Expense (Years Ending December 31)</b>	<b>Amount</b>
2011	\$ 203,999
2012	132,331
2013	117,444
2014	48,085
2015	30,329

**5. Accrued Expenses**

Accrued expenses consisted of the following:

	<b>December 31, 2010</b>	<b>March 31, 2011</b>
Marketing programs	\$ 3,265,692	\$ 2,069,731
Payroll and payroll related	4,535,322	2,940,553
Professional fees	745,834	1,228,635
Legal settlements (see Note 8)		1,250,000
Other accrued liabilities	2,282,462	2,323,094
<b>Total accrued expenses</b>	<b>\$ 10,829,310</b>	<b>\$ 9,812,013</b>

**6. Income Taxes**

The Company recorded a benefit for federal, state and foreign income taxes of approximately \$35,000 for the three months ended March 31, 2011. The Company's tax provision for the three months ended March 31, 2010 primarily consists of alternative minimum taxes and foreign income taxes, as well as a deferred provision related to the book and tax basis differences of goodwill. During the three months ended March 31, 2010, the Company maintained a full valuation allowance against all of its net deferred tax assets. However, the Company reversed the valuation allowance against primarily all of its net deferred tax assets at June 30, 2010 and therefore its tax provision and effective tax rate has increased year-over-year.

Deferred income taxes are provided for the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, and operating loss carry-forwards and credits using enacted tax rates expected to be in effect in the years in which the differences are expected to reverse. At each balance sheet date, the Company assesses the likelihood that deferred tax assets will be realized, and recognizes a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction. As of December 31, 2010 and March 31, 2011, the Company maintained a full valuation allowance related to the deferred tax assets of its Hungarian subsidiary.

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The Company's income tax returns since inception are open to examination by federal, state, and foreign tax authorities. The Company has no amount recorded for any unrecognized tax benefits as of December 31, 2010 or March 31, 2011. The Company's policy is to record estimated interest and penalty related to the underpayment of income taxes or unrecognized tax benefits as a component of its income tax provision. During the three months ended March 31, 2010 and 2011, the Company did not recognize any interest or penalties in its statements of operations, and there are no accruals for interest or penalties at December 31, 2010 or March 31, 2011.

The Company has performed an analysis of its ownership changes as defined by Section 382 of the Internal Revenue Code and has determined that an ownership change as defined by Section 382 occurred in October 2004 and March 2010 resulting in approximately \$219,000 and \$12,800,000, respectively, of net operating losses ( NOLs ) being subject to limitation. As of December 31, 2010 and March 31, 2011, the Company believes all NOLs generated by the Company, including those subject to limitation, are available for utilization given the Company's large annual limitation amount. Subsequent ownership changes as defined by Section 382 could potentially limit the amount of net operating loss carry-forwards that can be utilized annually to offset future taxable income.

#### **7. Stock Option Plans**

On June 9, 2009, the Company's Board of Directors approved the 2009 Stock Incentive Plan (the 2009 Plan ) which became effective upon the closing of the Company's initial public offering, or IPO. A total of 800,000 shares of common stock, subject to increase on an annual basis, were reserved for future issuance under the 2009 Plan. Shares of common stock reserved for issuance under the 2007 Stock Incentive Plan that remained available for issuance at the time of effectiveness of the 2009 Plan and any shares of common stock subject to awards under the 2007 Plan that expire, terminate, or are otherwise forfeited, canceled, or repurchased by the Company were added to the number of shares available under the 2009 Plan. The 2009 Plan is administered by the Board of Directors and Compensation Committee, which have the authority to designate participants and determine the number and type of awards to be granted, the time at which awards are exercisable, the method of payment and any other terms or conditions of the awards. Options generally vest over a four-year period and expire ten years from the date of grant. Certain

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options provide for accelerated vesting if there is a change in control. On January 1, 2010, subject to the provisions of the 2009 Plan, 448,996 shares were added to the shares available for grant under the 2009 Plan. On May 27, 2010, the Company's stockholders approved a 2,000,000 share increase to the shares available for grant under the 2009 Plan and removed the annual automatic share increase provision from the 2009 Plan. There were 1,760,803 shares available for grant under the 2009 Plan as of March 31, 2011.

The Company uses the Black-Scholes option-pricing model to estimate the grant date fair value of stock option grants. The Company estimates the expected volatility of its common stock at the date of grant based on the historical volatility of comparable public companies over the option's expected term as well as its own stock price volatility since the Company's IPO. The Company estimates expected term based on historical exercise activity and giving consideration to the contractual term of the options, vesting schedules, employee turnover, and expectation of employee exercise behavior. The assumed dividend yield is based upon the Company's expectation of not paying dividends in the foreseeable future. The risk-free rate for periods within the estimated life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Historical employee turnover data is used to estimate pre-vesting option forfeiture rates. The compensation expense is amortized on a straight-line basis over the requisite service period of the options, which is generally four years.

The Company used the following assumptions to apply the Black-Scholes option-pricing model:

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	2010	2011
Expected dividend yield	0.00%	0.00%
Risk-free interest rate	2.46%	2.28%
Expected term (in years)	6.25	5.56-6.25
Volatility	75%	60%

The following table summarizes stock option activity, including performance-based options:

	<b>Number of Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term (Years)</b>	<b>Aggregate Intrinsic Value</b>
Outstanding, January 1, 2011	2,564,315	\$ 12.76	7.3	\$ 80,983,495
Granted	649,550	40.07		
Exercised	(162,768)	7.17		\$ 5,068,951
Forfeited	(111,675)	28.26		
Outstanding, March 31, 2011	2,939,422	\$ 18.51	7.6	\$ 69,503,812
Exercisable at December 31, 2010	1,246,838	\$ 5.36	5.7	\$ 48,600,697
Exercisable at March 31, 2011	1,331,187	\$ 7.18	5.7	\$ 46,570,232

The aggregate intrinsic value was calculated based on the positive differences between the estimated fair value of the Company's common stock on December 31, 2010, of \$44.34, and \$42.16 per share on March 31, 2011, or at time of exercise, and the exercise price of the options.

The weighted average grant date fair value of stock options issued or modified was \$14.63 per share for the year ended December 31, 2010, and \$23.09 for the three months ended March 31, 2011.

The Company recognized stock based compensation expense within the accompanying condensed consolidated statements of operations as summarized in the following table:

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	<b>Three Months Ended, March 31,</b>	
	<b>2010</b>	<b>2011</b>
Cost of revenue	\$ 32,170	\$ 89,052
Research and development	135,963	280,116
Sales and marketing	235,520	562,535
General and administrative	623,146	813,791
	<b>\$ 1,026,799</b>	<b>\$ 1,745,494</b>

As of March 31, 2011, there was approximately \$23,415,000 of total unrecognized share-based compensation cost, net of estimated forfeitures, related to unvested stock option grants which are expected to be recognized over a weighted average period of 3.2 years. The total unrecognized share-based compensation cost will be adjusted for future changes in estimated forfeitures.

Of the total stock options issued subject to the plans, certain stock options have performance-based vesting. These performance-based options granted during 2004 and 2007 were granted at-the-money, contingently vest over a period of two to four years depending upon the nature of the performance goal, and have a contractual life of ten years. The performance-based stock option activity is summarized below:

	<b>Number of Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term (Years)</b>	<b>Aggregate Intrinsic Value</b>
Outstanding, January 1, 2011	532,932	\$ 1.25	4.6	\$ 22,964,040
Granted				
Exercised	(30,000)	1.25		1,143,000
Forfeited				
Outstanding, March 31, 2011	502,932	1.25	4.3	20,574,948
Exercisable at December 31, 2010	532,932	1.25	4.6	22,964,040
Exercisable at March 31, 2011	502,932	1.25	4.3	20,574,948

The aggregate intrinsic value was calculated based on the positive differences between the estimated fair value of the Company's common stock on December 31, 2010, of \$44.34 per share, and \$42.16 per share on March 31, 2011, or at the time of exercise, and the exercise price of the options.

**8. Commitments and Contingencies**

*Operating Leases* The Company has operating lease agreements for offices in Massachusetts, Hungary, The Netherlands, Australia and England that expire in 2012 through 2016. The lease agreement for the Massachusetts office requires a security deposit of \$125,000 in the form of a letter of credit which is collateralized by a certificate of deposit in the same amount. The lease agreement for one of the Company's Hungarian offices requires a security deposit, which totaled approximately \$239,068 (170,295 Euro) at March 31, 2011. The lease for the Company's Australian office requires a bank guarantee which totaled \$25,133 (24,375 AUD) at March 31, 2011, whereby the bank agrees to pay the lessor this amount should the Company default under the terms of the lease. The certificate of deposit, the security deposit and bank guarantee are classified as restricted cash. The Netherlands and Budapest, Hungary leases contain termination options which allow the Company to terminate the leases pursuant to certain lease provisions.

In February 2011, the Company entered into a lease for new office space for its Australian office. The term of the new office space began in February 2011 and extends through January 2014. The approximate annual lease payments for the new office space are \$91,000.

In April 2011, the Company entered into a lease for new office space for its England office. The term of the new office space began in April 2011 and extends through April 4, 2016. The approximate annual lease payments for the new office space are \$231,000. The lease contains a termination option which allows the Company to terminate the lease pursuant to certain lease provisions.

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Rent expense under all leases was approximately \$518,000 and \$660,000 for the three months ended March 31, 2010 and 2011, respectively. The Company records rent expense on a straight-line basis for leases with scheduled escalation clauses or free rent periods.

The Company also enters into hosting services agreements with third-party data centers and internet service providers that are subject to annual renewal. Hosting fees incurred under these arrangements aggregated approximately \$359,000 and \$496,000 for the three months ended March 31, 2010 and 2011, respectively.

Future minimum lease payments under non-cancelable operating leases including one year commitments associated with the Company's hosting services arrangements are approximately as follows at March 31, 2011:

**Years Ending December 31**

2011 (nine months ending December 31)	\$ 3,040,000
2012	2,912,000
2013	1,432,000
2014	375,000
2015	231,000
Thereafter	58,000
 Total minimum lease payments	 \$ 8,048,000

*Litigation* On September 8, 2010, 01 Communique Laboratory, Inc., or 01, filed a complaint that named the Company as a defendant in a lawsuit in the U.S. District Court for the Eastern District of Virginia (Civil Action No. 1:10cv1007). The Company received service of the complaint on September 10, 2010. The complaint alleged that the Company infringed U.S. Patent No. 6,928,479, which allegedly is owned by 01 and has claims directed to a particular application or system for providing a private communication portal from one computer to a second computer. The complaint sought damages in an unspecified amount and injunctive relief. On April 1, 2011, the U.S. District Court for the Eastern District of Virginia granted the Company's motion for summary judgment of non-infringement and the trial tentatively scheduled for the second quarter of 2011 was removed from the court's calendar. The Company expects the court will issue a written order regarding this decision. 01 has indicated that it intends to appeal the court's ruling granting summary judgment.

On November 3, 2010, Gemini IP LLC, or Gemini, filed a complaint that named the Company as a defendant in a lawsuit in the U.S. District Court for the Eastern District of Texas (Civil Action No. 4:07-cv-521). The Company received service of the complaint on November 10, 2010. The complaint alleged that the Company infringed U.S. Patent No. 6,117,932, which allegedly is owned by Gemini and has claims related to a system for operating an IT helpdesk. The complaint sought damages in an unspecified amount and injunctive relief. On April 25, 2011, the Company and Gemini entered into a License Agreement which granted the Company a fully-paid license that covers the patent at issue in the action and mutually released each party from all claims. The Company paid Gemini a one-time licensing fee of \$1,250,000 in connection with the License Agreement. As a result, the Company expects the action to be dismissed by the court in May 2011.

The Company is from time to time subject to various other legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these other claims cannot be predicted with certainty, management does not believe that the outcome of any of these other legal matters will have a material adverse effect on the Company's consolidated financial statements.

*Other Contingencies* The Company was contacted by a representative from a state tax assessor's office requesting remittance of uncollected sales taxes. The Company does not believe it was responsible for collecting sales taxes in this state and is investigating this request and intends to vigorously defend this position. If the Company does not prevail in its position, uncollected sales taxes due for the period from 2005 to the present could amount to approximately \$1.1 million excluding interest or penalties.

**9. Related Party Transactions**



In December 2007, the Company entered into a strategic connectivity service and marketing agreement with Intel Corporation to jointly develop a service that delivers connectivity to computers built with Intel components. Under the terms of the multi-year agreement, the Company adapted its service delivery platform, Gravity, to work with specific technology delivered with Intel hardware and software products. The agreement provided that Intel would market and sell the service to its customers. Intel paid the Company a minimum license and service fee on a quarterly basis during the multi-year term of the agreement. The Company began recognizing revenue associated with the Intel service and marketing agreement upon receipt of acceptance in the quarter ended September 30, 2008. In addition, the Company and Intel shared revenue generated by the use of the service by third parties to the extent it exceeded the minimum payments. In conjunction with this agreement, Intel Capital purchased 2,222,223 shares of the Company's Series B-1 redeemable convertible preferred stock for \$10,000,004, which were converted into 888,889 shares of common stock in connection with the closing of the IPO on July 7, 2009.

In September 2010, Intel notified the Company that it intended to terminate the connectivity service and marketing agreement effective on December 26, 2010. In accordance with the termination provisions of the agreement, Intel paid the Company a one-time termination fee of \$2.5 million in lieu of the \$5 million in annual fees associated with 2011. Intel paid the Company the \$2.5 million termination fee in December 2010.

At December 31, 2010 and March 31, 2011, Intel owed the Company approximately \$9,000 and \$0, respectively, recorded as a non-trade receivable relating to this agreement. The Company recognized approximately \$1,487,000 and \$0 of net revenue relating to these agreements for the three months ended March 31, 2010 and 2011, respectively. As of December 31, 2010 and March 31, 2011, the Company had recorded \$0 related to this agreement as deferred revenue.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the unaudited condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q and the audited consolidated financial statements and notes thereto and management's discussion and analysis of financial condition and results of operations for the year ended December 31, 2010 included in our Annual Report on Form 10-K, filed with the Securities and Exchange Commission, or SEC, on February 28, 2011. This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These statements are often identified by the use of words such as may, will, expect, believe, anticipate, intend, could, estimate, or continue, and similar expressions or variations. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in the section titled Risk Factors, set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and elsewhere in this Report. The forward-looking statements in this Quarterly Report on Form 10-Q represent our views as of the date of this Quarterly Report on Form 10-Q. We anticipate that subsequent events and developments will cause our views to change. However, while we may elect to update these forward-looking statements at some point in the future, we have no current intention of doing so except to the extent required by applicable law. You should, therefore, not rely on these forward-looking statements as representing our views as of any date subsequent to the date of this Quarterly Report on Form 10-Q.*

**Overview**

LogMeIn provides SaaS-based, on-demand, remote-connectivity, collaboration and support solutions to SMBs, IT service providers, mobile carriers, and consumers. Businesses and IT service providers use our solutions to deliver remote, end-user support and to access and manage computers and other Internet-enabled devices more effectively and efficiently from a remote location, or remotely. Consumers and mobile workers use our remote connectivity solutions to access computer resources remotely and to collaborate with other users, thereby facilitating their mobility and increasing their productivity. SMBs and mobile professionals use our solutions to meet online and quickly collaborate on projects. Our solutions, which are deployed and accessed from anywhere through a web browser, or on-demand, are secure, scalable and easy for our customers to try, purchase and use.

We offer three free services and nine premium services. Sales of our premium services are generated through word-of-mouth referrals, web-based advertising, expiring free trials that we convert to paid subscriptions and direct marketing to new and existing customers.

We derive our revenue principally from subscription fees from SMBs, IT service providers, mobile carriers and consumers. The majority of our customers subscribe to our services on an annual basis. Our revenue is driven primarily by the number and type of our premium services for which our paying customers subscribe. For the three months ended March 31, 2011, we generated revenues of \$27.0 million, compared to \$21.3 million for the three months ended March 31, 2010, an increase of approximately 27%. In fiscal 2010, we generated revenues of \$101.1 million.

**Certain Trends and Uncertainties**

The following represents a summary of certain trends and uncertainties, which could have a significant impact on our financial condition and results of operations. This summary is not intended to be a complete list of potential trends and uncertainties that could impact our business in the long or short term. The summary, however, should be considered along with the factors identified in the section titled Risk Factors set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and elsewhere in this report.

We continue to closely monitor current adverse economic conditions, particularly as they impact SMBs, IT service providers and consumers. We are unable to predict the likely duration and severity of the current adverse economic conditions in the United States and other countries, but the longer the duration the greater risks we face in operating our business.

We believe that competition will continue to increase. Increased competition could result from existing competitors or new competitors

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that enter the market because of the potential opportunity. We will continue to closely monitor competitive activity and respond accordingly. Increased competition could have an adverse effect on our financial condition and results of operations.

We believe that as we continue to grow revenue at expected rates, our cost of revenue and operating expenses, including sales and marketing, research and development and general and administrative expenses will increase in absolute dollar amounts. For a description of the general trends we anticipate in various expense categories, see Cost of Revenue and Operating Expenses below.

**Sources of Revenue**

We derive our revenue principally from subscription fees from SMBs, IT service providers, mobile carriers and consumers. Our revenue is driven primarily by the number and type of our premium services for which our paying customers subscribe and is not concentrated within one customer or group of customers. The majority of our customers subscribe to our services on an annual basis and pay in advance, typically with a credit card, for their subscription. A smaller percentage of our customers subscribe to our services on a monthly basis through either month-to-month commitments or annual commitments that are then paid monthly with a credit card. We initially record a subscription fee as deferred revenue and then recognize it ratably, on a daily basis, over the life of the subscription period. Typically, a subscription automatically renews at the end of a subscription period unless the customer specifically terminates it prior to the end of the period.

In addition to our subscription fees, to a lesser extent, we also generate revenue from license and annual maintenance fees from the licensing of our RemotelyAnywhere product. We license RemotelyAnywhere to our customers on a perpetual basis. Because we do not have vendor specific objective evidence of fair value, or VSOE, for our maintenance arrangements, we record the initial license and maintenance fee as deferred revenue and recognize the fees as revenue ratably, on a daily basis, over the initial maintenance period. We also initially record maintenance fees for subsequent maintenance periods as deferred revenue and recognize revenue ratably, on a daily basis, over the maintenance period. We also generate revenue from the license of our Ignition for iPhone, iPad and Android product which is sold as a perpetual license and is recognized as delivered. Revenue from RemotelyAnywhere, Ignition for iPhone, iPad and Android represented approximately 7% of our revenue for the three months ended March 31, 2011.

**Employees**

We have increased our number of full-time employees to 417 at March 31, 2011 as compared to 415 at December 31, 2010 and 353 at March 31, 2010.

**Cost of Revenue and Operating Expenses**

We allocate certain overhead expenses, such as rent and utilities, to expense categories based on the headcount in or office space occupied by personnel in that expense category as a percentage of our total headcount or office space. As a result, an overhead allocation associated with these costs is reflected in the cost of revenue and each operating expense category.

*Cost of Revenue.* Cost of revenue consists primarily of costs associated with our data center operations and customer support centers, including wages and benefits for personnel, telecommunication and hosting fees for our services, equipment maintenance, maintenance and license fees for software licenses and depreciation. Additionally, amortization expense associated with the acquired software and technology as well as internally developed software is included in cost of revenue. The expenses related to hosting our services and supporting our free and premium customers is related to the number of customers who subscribe to our services and the complexity and redundancy of our services and hosting infrastructure. We expect these expenses to increase in absolute dollars as we continue to increase our number of customers over time but, in total, to remain relatively constant as a percentage of revenue.

*Research and Development.* Research and development expenses consist primarily of wages and benefits for development personnel, professional fees associated with outsourced development projects and depreciation associated with assets used in development. We have focused our research and development efforts on both improving ease of use and functionality of our existing services, as well as developing new offerings. The majority of our research and development employees are located in our development centers in Hungary. Therefore, a majority of research and development expense is subject to fluctuations in foreign exchange rates. During the three months ended

March 31, 2011, we capitalized approximately \$0.1 million of costs related to internally developed computer software to be sold as a service, which was incurred during the application development stage. No amounts were capitalized for the three months ended March 31, 2010 as the costs incurred during such stage were immaterial. As a result, the majority of research and development costs have been expensed as incurred. We expect that research and development expenses will increase in both absolute dollars and as a percentage of revenue as we continue to enhance and expand our services.

*Sales and Marketing.* Sales and marketing expenses consist primarily of online search and advertising costs, wages, commissions and benefits for sales and marketing personnel, offline marketing costs such as media advertising and trade shows, professional fees and credit card processing fees. Online search and advertising costs consist primarily of pay-per-click payments to search engines and other online advertising media such as banner ads. Offline marketing costs include radio and print advertisements as well as the costs to create and produce these advertisements, and tradeshows, including the costs of space at tradeshows and costs to design and construct tradeshow booths. Advertising costs are expensed as incurred. In order to continue to grow our business and awareness of our services, we expect that we will continue to

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commit resources to our sales and marketing efforts. We expect that sales and marketing expenses will increase in absolute dollars but decrease as a percentage of revenue over time as our revenue increases.

*General and Administrative.* General and administrative expenses consist primarily of wages and benefits for management, human resources, internal IT support, finance and accounting personnel, professional fees, insurance and other corporate expenses. We expect that general and administrative expenses will decrease significantly primarily due to a reduction in the legal costs associated with our defense against the patent infringement claims made by 01 Communique. Additionally, general and administrative expenses will increase as we continue to add personnel, enhance our internal information systems to align with the growth of our business and expenses related to audit, accounting and insurance costs. We expect that our general and administrative expenses will significantly decrease in both absolute dollars and as a percentage of revenue when compared to the quarter ended March 31, 2011 and increase in absolute dollars but remain constant as a percentage of revenue as compared to prior historical quarters.

**Critical Accounting Policies**

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of our financial statements and related disclosures requires us to make estimates, assumptions and judgments that affect the reported amount of assets, liabilities, revenue, costs and expenses, and related disclosures. We base our estimates and assumptions on historical experience and other factors that we believe to be reasonable under the circumstances. We evaluate our estimates and assumptions on an ongoing basis. Our actual results may differ from these estimates under different assumptions and conditions. Our most critical accounting policies are listed below:

Revenue recognition;

Income taxes;

Stock-based compensation; and

Loss contingencies.

During the three months ended March 31, 2011, there were no significant changes in our critical accounting policies or estimates. See Notes 2, 6, 7 and 8 to our condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q and included in our Annual Report on Form 10-K for the year ended December 31, 2010, as filed with the SEC on February 28, 2011, for additional information about these critical accounting policies, as well as a description of our other significant accounting policies.

**Results of Consolidated Operations**

The following table sets forth selected consolidated statements of operations data for each of the periods indicated as a percentage of total revenue.

	<b>Three Months Ended March 31,</b>	
	<b>2010</b>	<b>2011</b>
Revenue	100%	100%
Cost of revenue	10	9
Gross profit	90	91
Operating expenses:		
Research and development	17	16
Sales and marketing	46	48

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General and administrative	13	22
Legal settlements		5
Amortization of acquired intangibles		
Total operating expenses	76	91
Income (loss) from operations	13	
Interest and other (income) expense, net		
Income (loss) before provision for income taxes	13	
(Provision) benefit for income taxes		
Net income (loss)	13%	%
<b>Three Months Ended March 31, 2011 and 2010</b>		

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*Revenue.* Revenue for the three months ended March 31, 2011 was \$27.0 million, an increase of \$5.7 million, or 27%, over revenue of \$21.3 million for the three months ended March 31, 2010. Of the 27% increase in revenue, the majority of the increase was due to an increase in revenue from new customers, as our total number of premium accounts increased to approximately 685,000 at March 31, 2011 from approximately 340,000 premium accounts at March 31, 2010, and incremental add-on revenues from our existing customer base. Included in the revenue for the three months ended March 31, 2010 was \$1.5 million related to the service and marketing agreement with Intel compared to \$0 for the three months ended March 31, 2011.

*Cost of Revenue.* Cost of revenue for the three months ended March 31, 2011 was \$2.5 million, an increase of \$0.3 million, or 14%, over cost of revenue of \$2.2 million for the three months ended March 31, 2010. As a percentage of revenue, cost of revenue was 9% and 10% for the three months ended March 31, 2011 and 2010, respectively. The increase in absolute dollars resulted primarily from an increase in both the number of customers using our premium services and the total number of devices that connected to our services, including devices owned by free users, which resulted in increased hosting and customer support costs. Of the increase in cost of revenue, \$0.2 million resulted from increased data center costs associated with managing our data centers and the hosting of our services. The increase in data center costs was due to the expansion of our data center facilities as we added capacity to our hosting infrastructure. Additionally, \$0.2 million of the increase in cost of revenue was due to the increased costs in our customer support organization, primarily as a result of hiring new employees to support our customer growth.

*Research and Development Expenses.* Research and development expenses for the three months ended March 31, 2011 were \$4.3 million, an increase of \$0.8 million, or 22%, over research and development expenses of \$3.6 million for the three months ended March 31, 2010. As a percentage of revenue, research and development expenses were 16% and 17% for the three months ended March 31, 2011 and 2010, respectively. The increase in absolute dollars was primarily due to a \$0.6 million increase in personnel-related costs as we hired additional employees to improve the ease of use and functionality of our existing services as well as develop new service offerings. The increase in personnel-related costs was offset by the capitalization of approximately \$0.1 million of costs incurred during the application development stage related to new product development and development of significant new functionality to existing products during the three months ended March 31, 2011. No amounts were capitalized during the three months ended March 31, 2010 as the costs incurred in the period were immaterial.

*Sales and Marketing Expenses.* Sales and marketing expenses for the three months ended March 31, 2011 were \$13.0 million, an increase of \$3.1 million, or 32%, over sales and marketing expenses of \$9.8 million for the three months ended March 31, 2010. As a percentage of revenue, sales and marketing expenses were 48% and 46% for the three months ended March 31, 2011 and 2010, respectively. The increase in absolute dollars was primarily due to a \$1.6 million increase in marketing program costs and a \$1.2 million increase in personnel-related and recruiting costs from additional employees hired to support our growth in sales and expand our marketing efforts. The increase was also due to a \$0.1 million increase in credit card processing fees, a \$0.1 million increase in travel-related costs and a \$0.1 million increase in rent costs primarily related to the expansion of our corporate headquarters.

*General and Administrative Expenses.* General and administrative expenses for the three months ended March 31, 2011 were \$6.1 million, an increase of \$3.3 million, or 116%, over general and administrative expenses of \$2.8 million for the three months ended March 31, 2010. As a percentage of revenue, general and administrative expenses were 22% and 13% for the three months ended March 31, 2011 and 2010, respectively. The increase in absolute dollars was primarily due to a \$2.9 million increase in legal costs associated with our defense against the patent infringement claims made by 01 Communique. The increase was also due to \$0.4 million increase in personnel-related costs as we increased the number of general and administrative employees to support our overall growth.

*Legal Settlement Expenses.* Legal settlement expenses were \$1.3 million for the three months ended March 31, 2011, compared to \$0 for the three months ended March 31, 2010. The legal settlement expenses for the three months ended March 31, 2011 are related to the License Agreement entered into by the Company and Gemini IP LLC on April 25, 2011 (see Note 8).



*Amortization of Acquired Intangibles.* Amortization of acquired intangibles for the three months ended March 31, 2011 and 2010 was \$0.1 million and related primarily to the value of intangible assets acquired in our July 2006 acquisition of Applied Networking, Inc.

*Interest Income, Net.* Interest income, net for the three months ended March 31, 2011 was income of approximately \$0.2 million, compared to income of approximately \$0.1 million for the three months ended March 31, 2010. The change was mainly due to an increase in interest income resulting from an increase in the balance of funds invested in higher yielding marketable securities.

*Other Expense.* Other expense for the three months ended March 31, 2011 and 2010 was \$0.1 million and related to foreign currency losses.

*Income Taxes.* During the three months ended March 31, 2011, we recorded a benefit for federal, state and foreign income taxes of approximately \$35,000. For the three months ended March 31, 2010, we recorded a provision primarily for alternative minimum taxes and foreign income taxes, as well as a deferred provision related to the book and tax basis differences of goodwill of approximately \$0.1 million. During the three months ended March 31, 2010, we maintained a full valuation allowance against all of our net deferred tax assets. However, we reversed the valuation allowance against primarily all of our net deferred tax assets at June 30, 2010 and therefore our tax provision and effective tax rate has increased year-over-year. At each balance sheet date, we assesses the likelihood that deferred tax assets will be realized, and recognize a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction. As of December 31, 2010 and March 31, 2011, we maintained a full valuation allowance related to the deferred tax assets of our Hungarian subsidiary due to its historical net losses.

**Table of Contents****Liquidity and Capital Resources**

The following table sets forth the major sources and uses of cash for each of the periods set forth below:

	<b>Three Months Ended March 31,</b>	
	<b>2010</b>	<b>2011</b>
	<b>(In thousands)</b>	
Net cash provided by operations	\$ 7,382	\$ 8,394
Net cash used in investing activities	(30,696)	(1,282)
Net cash provided by financing activities	1,140	1,118
Effect of exchange rate changes	(134)	572
Net increase (decrease) in cash	\$ (22,308)	\$ 8,802

At March 31, 2011, our principal source of liquidity was cash and cash equivalents and short-term marketable securities totaling \$176.2 million.

**Cash Flows From Operating Activities**

Net cash inflows from operating activities during the three months ended March 31, 2011 were mainly due to a \$4.8 million increase in deferred revenue associated with the increase in subscription sales orders and customer growth. Net cash inflows from operating activities were also due to non-cash operating expenses, including \$1.0 million for depreciation and amortization and \$1.8 million for stock compensation. The net cash inflows from operating activities were also due to a \$1.6 million increase in current liabilities and a \$0.5 million decrease in prepaid expenses and other current assets. These were offset by a \$1.1 million increase in accounts receivable. We expect that our future cash flows from operating activities will be impacted by the legal costs associated with our defense against the patent infringement claim made by 01 Communique.

Net cash inflows from operating activities during the three months ended March 31, 2010 were mainly due to \$2.7 million of net income for the period, non-cash operating expenses, including \$0.9 million for depreciation and amortization and \$1.0 million for stock compensation, as well as a \$0.8 million decrease in accounts receivable, a \$0.2 million decrease in prepaid expenses and other current assets, a \$2.3 million increase in deferred revenue associated with the increase in subscription sales orders and a \$0.3 million increase in accounts payable, offset by a \$0.9 million decrease in accrued liabilities.

**Cash Flows From Investing Activities**

Net cash used in investing for the three months ended March 31, 2011 was primarily related to the addition of \$1.1 million in property and equipment mainly related to the expansion and upgrade of our data center capacity and also related to the expansion and upgrade of our internal IT infrastructure. Net cash used in investing activities was also related to the purchase of \$30.1 million of marketable securities offset by proceeds of \$30.0 million from sale or disposal of marketable securities.

Net cash used in investing activities during the three months ended March 31, 2010 was mainly due to the purchase of \$55.3 million of marketable securities offset by proceeds of \$25.0 million from maturity of marketable securities. Net cash used in investing activities was also due to \$0.4 million from purchases of property and equipment mainly for use in our existing data centers.

Our future capital requirements may vary materially from those currently planned and will depend on many factors, including, but not limited to, development of new services, market acceptance of our services, the expansion of our sales, support, development and marketing organizations, the establishment of additional offices in the United States and worldwide and the expansion of our data center infrastructure necessary to support our growth. Since our inception, we have experienced increases in our expenditures consistent with the growth in our operations and personnel, and we anticipate that our expenditures will continue to increase in the future. We also intend to make investments in computer equipment and systems and infrastructure related to existing and new offices as we move and

expand our facilities, add additional personnel and continue to grow our business. We are not currently party to any purchase contracts related to future capital expenditures.

***Cash Flows From Financing Activities***

Net cash flows provided by financing activities were \$1.1 million for the three months ended March 31, 2011 and were related to proceeds received from the issuance of common stock upon exercise of stock options.

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Net cash provided by financing activities for the three months ended March 31, 2010 was due to \$1.3 million in proceeds received from the issuance of common stock upon exercise of stock options offset by \$0.2 million in payments made in connection with our secondary public offering.

While we believe that our current cash and cash equivalents will be sufficient to meet our working capital and capital expenditure requirements for at least the next twelve months, we may elect to raise additional capital through the sale of additional equity or debt securities or obtain a credit facility to develop or enhance our services, to fund expansion, to respond to competitive pressures or to acquire complementary products, businesses or technologies. If we elect, additional financing may not be available in amounts or on terms that are favorable to us, if at all. If we raise additional funds through the issuance of equity or convertible debt securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock.

During the last three years, inflation and changing prices have not had a material effect on our business and we do not expect that inflation or changing prices will materially affect our business in the foreseeable future.

**Off-Balance Sheet Arrangements**

We do not engage in any off-balance sheet financing activities, nor do we have any interest in entities referred to as variable interest entities.

**Table of Contents****Contractual Obligations**

The following table summarizes our contractual obligations at March 31, 2011 and the effect such obligations are expected to have on our liquidity and cash flow in future periods.

	<b>Payments Due by Period</b>				<b>More Than 5 Years</b>
	<b>Total</b>	<b>Less Than 1 Year</b>	<b>1-3 Years</b>	<b>3-5 Years</b>	
Operating lease obligations	\$ 7,119,000	\$ 2,905,000	\$ 3,752,000	\$ 462,000	\$
Hosting service agreements	929,000	929,000			
<b>Total</b>	<b>\$ 8,048,000</b>	<b>\$ 3,834,000</b>	<b>\$ 3,752,000</b>	<b>\$ 462,000</b>	<b>\$</b>

The commitments under our operating leases shown above consist primarily of lease payments for our Woburn, Massachusetts corporate headquarters, our international sales and marketing offices located in The Netherlands, Australia and England and our research and development offices in Hungary and contractual obligations related to our data centers.

The table above includes the leases for our new spaces for our Australia and England offices. In February 2011, we entered into a lease for new office space for our Australian office. The term of the new office space began in February 2011 and extends through January 2014. The approximate annual lease payments for the new office space are \$91,000. In April 2011, we entered into a lease for new office space for our England office. The term of the new office space began in April 2011 and extends through April 4, 2016. The approximate annual lease payments for the new office space are \$231,000.

**Recent Accounting Pronouncements**

In October 2009, an update was made to Revenue Recognition Multiple Deliverable Revenue Arrangements. This update removes the objective-and-reliable-evidence-of-fair-value criterion from the separation criteria used to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting, replaces references to fair value with selling price to distinguish from the fair value measurements required under the Fair Value Measurements and Disclosures guidance, provides a hierarchy that entities must use to estimate the selling price, eliminates the use of the residual method for allocation, and expands the ongoing disclosure requirements. The effect of adoption of this standard has only impacted our financial statement disclosure to comply with the additional disclosure requirements as described in Note 2 to the condensed consolidated financial statements. The implementation of this guidance did not have a material impact on our consolidated financial position, results of operations or cash flows.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

*Foreign Currency Exchange Risk.* Our results of operations and cash flows are subject to fluctuations due to changes in foreign currency exchange rates as a result of the majority of our research and development expenditures being made from our Hungarian research and development facilities, and in our international sales and marketing offices in The Netherlands, England, Australia and Brazil. In the three months ended March 31, 2011, approximately 13%, 4%, 3%, 2% and less than 1% of our operating expenses occurred in our operations in Hungary, The Netherlands, England, Australia and Brazil, respectively. In the three months ended March 31, 2010, approximately 16%, 12%, 1% and 3% of our operating expenses occurred in our operations in Hungary, The Netherlands, England and Australia, respectively.

Additionally, an increasing percentage of our sales outside the United States are denominated in local currencies and, thus, are also subject to fluctuations due to changes in foreign currency exchange rates. To date, changes in foreign currency exchange rates have not had a material impact on our operations, and a future change of 20% or less in foreign currency exchange rates would not materially affect our operations. At this time, we do not, but may in the

future, enter into any foreign currency hedging programs or instruments that would hedge or help offset such foreign currency exchange rate risk.

*Interest Rate Sensitivity.* Interest income is sensitive to changes in the general level of U.S. interest rates. However, based on the nature and current level of our cash and cash equivalents, which are primarily invested in deposits and money market funds, we believe there is no material risk of exposure to changes in the fair value of our cash and cash equivalents as a result of changes in interest rates.

#### **ITEM 4. CONTROLS AND PROCEDURES**

*Evaluation of Disclosure Controls and Procedures.* Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of March 31, 2011. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and

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procedures. Based on the evaluation of our disclosure controls and procedures as of March 31, 2011, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

*Changes in Internal Controls.* No changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the quarter ended March 31, 2011 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

On September 8, 2010, 01 Communique Laboratory, Inc., or 01, filed a complaint that named us as a defendant in a lawsuit in the U.S. District Court for the Eastern District of Virginia (Civil Action No. 1:10cv1007). We received service of the complaint on September 10, 2010. The complaint alleged that we infringed U.S. Patent No. 6,928,479, which allegedly is owned by 01 and has claims directed to a particular application or system for providing a private communication portal from one computer to a second computer. The complaint sought damages in an unspecified amount and injunctive relief. On April 1, 2011, the U.S. District Court for the Eastern District of Virginia granted our motion for summary judgment of non-infringement and the trial tentatively scheduled for the second quarter of 2011 was removed from the court's calendar. We expect the court will issue a written order regarding this decision. 01 has indicated that it intends to appeal the court's ruling granting summary judgment.

On November 3, 2010, Gemini IP LLC, or Gemini, filed a complaint that named us as a defendant in a lawsuit in the U.S. District Court for the Eastern District of Texas (Civil Action No. 4:07-cv-521). We received service of the complaint on November 10, 2010. The complaint alleged that we infringed U.S. Patent No. 6,117,932, which allegedly is owned by Gemini and has claims related to a system for operating an IT helpdesk. The complaint sought damages in an unspecified amount and injunctive relief. On April 25, 2011, we entered into a License Agreement with Gemini which granted us a fully-paid license that covers the patent at issue in the action and mutually released each party from all claims. We paid Gemini a one-time licensing fee of \$1,250,000 in connection with the License Agreement. As a result, we expect the action to be dismissed by the court in May of 2011.

We are from time to time subject to various legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these other claims cannot be predicted with certainty, management does not believe that the outcome of any of these other legal matters will have a material adverse effect on our consolidated financial statements.

**Item 1A. Risk Factors**

*Our business is subject to numerous risks. We caution you that the following important factors, among others, could cause our actual results to differ materially from those expressed in forward-looking statements made by us or on our behalf in filings with the SEC, press releases, communications with investors and oral statements. Any or all of our forward-looking statements in this Quarterly Report on Form 10-Q and in any other public statements we make may turn out to be wrong. They can be affected by inaccurate assumptions we might make or by known or unknown risks and uncertainties. Many factors mentioned in the discussion below will be important in determining future results. Consequently, no forward-looking statement can be guaranteed. Actual future results may differ materially from those anticipated in forward-looking statements. We undertake no obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosure we make in our reports filed with the SEC.*

**RISKS RELATED TO OUR BUSINESS*****We may be unable to achieve or maintain profitability.***

We experienced net losses of \$9.1 million for 2007, and \$5.4 million for 2008. In the quarter ended September 30, 2008, we achieved profitability and reported net income for the first time. We reported net income of \$8.8 million for 2009 and \$21.1 million for 2010. For the three months ended March 31, 2011, we experienced a net loss of \$0.1 million due primarily to patent litigation defense costs and costs related to a one-time legal settlement. We cannot predict if we will again achieve profitability or sustain profitability if achieved. We expect to continue making significant future expenditures to develop and expand our business. In addition, as a public company, we incur additional significant legal, accounting and other expenses that we did not incur as a private company. These

increased expenditures make it harder for us to maintain future profitability. Our recent growth in revenue and customer base may not be sustainable, and we may not achieve sufficient revenue to achieve or maintain profitability. We may incur significant losses in the future for a number of reasons, including due to the other risks described in this report and we may encounter unforeseen expenses, difficulties, complications and delays and other unknown events. Accordingly, we may not be able to again achieve or maintain profitability, and we may incur significant losses for the foreseeable future.

***Growth of our business may be adversely affected if businesses, IT support providers or consumers do not adopt remote access or remote support solutions more widely.***

Our services employ new and emerging technologies for remote access and remote support. Our target customers may hesitate to accept the risks inherent in applying and relying on new technologies or methodologies to supplant traditional methods of remote connectivity. Our business will not be successful if our target customers do not accept the use of our remote access and remote support technologies.



**Table of Contents*****Assertions by a third party that our services infringe its intellectual property, whether or not correct, could subject us to costly and time-consuming litigation or expensive licenses.***

There is frequent litigation in the software and technology industries based on allegations of infringement or other violations of intellectual property rights. We have been, and may in the future be, subject to third party patent infringement lawsuits as we face increasing competition and become increasingly visible. Regardless of the merit of these claims, they can be time-consuming, result in costly litigation and diversion of technical and management personnel or require us to develop a non-infringing technology or enter into license agreements. There can be no assurance that such licenses will be available on acceptable terms and conditions, if at all and although we have previously licensed proprietary technology, we cannot be certain that the owners' rights in such technology will not be challenged, invalidated or circumvented. For these reasons and because of the potential for high court awards that are difficult to predict, it is not unusual to find even arguably unmeritorious claims settled for significant amounts. In addition, many of our service agreements require us to indemnify our customers from certain third-party intellectual property infringement claims, which could increase our costs as a result of defending such claims and may require that we pay damages if there were an adverse ruling related to any such claims. These types of claims could harm our relationships with our customers, deter future customers from subscribing to our services or expose us to further litigation. Any adverse determination related to intellectual property claims or litigation could prevent us from offering all or a portion of our services to customers due to an injunction or require us to pay damages or license fees, which could adversely affect our business, financial condition and operating results.

For information concerning pending patent infringement cases in which we are involved, please refer to Part II, Item 1 entitled "Legal Proceedings" and Note 8 of the Notes to Condensed Consolidated Financial Statements.

***We depend on search engines to attract a significant percentage of our customers, and if those search engines change their listings or increase their pricing, it would limit our ability to attract new customers.***

Many of our customers locate our website through search engines, such as Google. Search engines typically provide two types of search results, algorithmic and purchased listings, and we rely on both types.

Algorithmic listings cannot be purchased and are determined and displayed solely by a set of formulas designed by the search engine. Search engines revise their algorithms from time to time in an attempt to optimize search result listings. If the search engines on which we rely for algorithmic listings modify their algorithms in a manner that reduces the prominence of our listing, fewer potential customers may click through to our website, requiring us to resort to other costly resources to replace this traffic. Any failure to replace this traffic could reduce our revenue and increase our costs. In addition, costs for purchased listings have increased in the past and may increase in the future, and further increases could have negative effects on our financial condition.

***If we are unable to attract new customers to our services on a cost-effective basis, our revenue and results of operations will be adversely affected.***

We must continue to attract a large number of customers on a cost-effective basis, many of whom have not previously used on-demand, remote-connectivity solutions. We rely on a variety of marketing methods to attract new customers to our services, such as paying providers of online services and search engines for advertising space and priority placement of our website in response to Internet searches. Our ability to attract new customers also depends on the competitiveness of the pricing of our services. If our current marketing initiatives are not successful or become unavailable, if the cost of such initiatives were to significantly increase, or if our competitors offer similar services at lower prices, we may not be able to attract new customers on a cost-effective basis and, as a result, our revenue and results of operations would be adversely affected.

***If we are unable to retain our existing customers, our revenue and results of operations would be adversely affected.***

We sell our services pursuant to agreements that are generally one year in duration. Our customers have no obligation to renew their subscriptions after their subscription period expires, and these subscriptions may not be renewed on the same or on more profitable terms. As a result, our ability to grow depends in part on subscription renewals. We may not be able to accurately predict future trends in customer renewals, and our customers' renewal rates may decline or fluctuate because of several factors, including their satisfaction or dissatisfaction with our services, the prices of our services, the prices of services offered by our competitors or reductions in our customers

spending levels. If our customers do not renew their subscriptions for our services, renew on less favorable terms, or do not purchase additional functionality or subscriptions, our revenue may grow more slowly than expected or decline, and our profitability and gross margins may be harmed.

***If we fail to convert our free users to paying customers, our revenue and financial results will be harmed.***

A significant portion of our user base utilizes our services free of charge through our free services or free trials of our premium services. We seek to convert these free and trial users to paying customers of our premium services. If our rate of conversion suffers for any reason, our revenue may decline and our business may suffer.

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***We may expand by acquiring or investing in other companies, which may divert our management's attention, result in additional dilution to our stockholders and consume resources that are necessary to sustain our business.***

Our business strategy may include acquiring complementary services, technologies or businesses. We also may enter into relationships with other businesses to expand our portfolio of services or our ability to provide our services in foreign jurisdictions, which could involve preferred or exclusive licenses, additional channels of distribution, discount pricing or investments in other companies. Negotiating these transactions can be time-consuming, difficult and expensive, and our ability to close these transactions may often be subject to conditions or approvals that are beyond our control. Consequently, these transactions, even if undertaken and announced, may not close.