

QUINSTREET, INC  
Form 10-Q  
February 06, 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 December 31, 2014**

**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 No. 001-34628**

**QuinStreet, Inc.**

**(Exact Name of Registrant as Specified in Its Charter)**

**Delaware**  
**(State or Other Jurisdiction of**  
**Incorporation or Organization)**

**77-0512121**  
**(I.R.S. Employer**  
**Identification No.)**

**950 Tower Lane, 6th Floor**

**Foster City, California**  
**(Address of principal executive offices)**

**94404**  
**(Zip Code)**

**650-578-7700**

**Registrant's telephone number, including area code**

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

Number of shares of common stock outstanding as of January 31, 2015: 44,492,160

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**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****QUINSTREET, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share and per share data)****(Unaudited)**

|                                            | <b>December 31,<br/>2014</b> | <b>June 30,<br/>2014</b> |
|--------------------------------------------|------------------------------|--------------------------|
| <b>Assets</b>                              |                              |                          |
| Current assets                             |                              |                          |
| Cash and cash equivalents                  | \$ 87,940                    | \$ 84,177                |
| Marketable securities                      | 27,951                       | 38,630                   |
| Accounts receivable, net                   | 41,115                       | 41,979                   |
| Deferred tax assets                        | 223                          | 223                      |
| Prepaid expenses and other assets          | 11,668                       | 11,647                   |
| Total current assets                       | 168,897                      | 176,656                  |
| Property and equipment, net                | 9,405                        | 11,126                   |
| Goodwill                                   | 55,451                       | 55,451                   |
| Other intangible assets, net               | 24,305                       | 31,441                   |
| Deferred tax assets, noncurrent            | 1,710                        | 1,712                    |
| Other assets, noncurrent                   | 479                          | 457                      |
| Total assets                               | \$ 260,247                   | \$ 276,843               |
| <b>Liabilities and Stockholders Equity</b> |                              |                          |
| Current liabilities                        |                              |                          |
| Accounts payable                           | \$ 21,610                    | \$ 19,517                |
| Accrued liabilities                        | 23,328                       | 27,854                   |
| Deferred revenue                           | 1,353                        | 1,175                    |
| Debt                                       | 19,714                       | 17,698                   |
| Total current liabilities                  | 66,005                       | 66,244                   |
| Debt, noncurrent                           | 49,764                       | 59,565                   |
| Other liabilities, noncurrent              | 5,630                        | 5,883                    |
| Total liabilities                          | 121,399                      | 131,692                  |

## Commitments and contingencies (See Note 8)

## Stockholders' equity

Common stock: \$0.001 par value; 100,000,000 shares authorized; 44,485,717 and 44,025,908 shares issued and outstanding at December 31, 2014 and June 30, 2014, respectively

|                                                   |                   |                   |
|---------------------------------------------------|-------------------|-------------------|
|                                                   | 44                | 44                |
| Additional paid-in capital                        | 244,777           | 239,558           |
| Accumulated other comprehensive loss              | (812)             | (1,054)           |
| Accumulated deficit                               | (105,161)         | (93,397)          |
| <b>Total stockholders' equity</b>                 | <b>138,848</b>    | <b>145,151</b>    |
| <b>Total liabilities and stockholders' equity</b> | <b>\$ 260,247</b> | <b>\$ 276,843</b> |

See notes to condensed consolidated financial statements

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|                                                              | <b>Three Months Ended<br/>December 31,</b> |             | <b>Six Months Ended<br/>December 31,</b> |             |
|--------------------------------------------------------------|--------------------------------------------|-------------|------------------------------------------|-------------|
|                                                              | <b>2014</b>                                | <b>2013</b> | <b>2014</b>                              | <b>2013</b> |
| Net revenue                                                  | \$ 66,694                                  | \$ 66,145   | \$ 135,883                               | \$ 143,106  |
| Cost of revenue <sup>(1)</sup>                               | 60,395                                     | 56,116      | 123,804                                  | 119,708     |
| Gross profit                                                 | 6,299                                      | 10,029      | 12,079                                   | 23,398      |
| Operating expenses: <sup>(1)</sup>                           |                                            |             |                                          |             |
| Product development                                          | 4,244                                      | 4,776       | 9,200                                    | 9,935       |
| Sales and marketing                                          | 3,357                                      | 3,659       | 7,024                                    | 7,815       |
| General and administrative                                   | 4,079                                      | 4,411       | 8,694                                    | 8,545       |
| Operating loss                                               | (5,381)                                    | (2,817)     | (12,839)                                 | (2,897)     |
| Interest income                                              | 28                                         | 27          | 54                                       | 54          |
| Interest expense                                             | (786)                                      | (976)       | (1,966)                                  | (2,002)     |
| Other income (expense), net                                  | 636                                        | (29)        | 2,961                                    | (48)        |
| Loss before income taxes                                     | (5,503)                                    | (3,795)     | (11,790)                                 | (4,893)     |
| Benefit from (provision for) taxes                           | 26                                         | (40,234)    | 26                                       | (40,075)    |
| Net loss                                                     | \$ (5,477)                                 | \$ (44,029) | \$ (11,764)                              | \$ (44,968) |
| Net loss per share:                                          |                                            |             |                                          |             |
| Basic                                                        | \$ (0.12)                                  | \$ (1.01)   | \$ (0.27)                                | \$ (1.04)   |
| Diluted                                                      | \$ (0.12)                                  | \$ (1.01)   | \$ (0.27)                                | \$ (1.04)   |
| Weighted average shares used in computing net loss per share |                                            |             |                                          |             |
| Basic                                                        | 44,440                                     | 43,420      | 44,353                                   | 43,268      |
| Diluted                                                      | 44,440                                     | 43,420      | 44,353                                   | 43,268      |

<sup>(1)</sup> Cost of revenue and operating expenses include stock-based compensation expense as follows:

|                            |        |        |          |          |
|----------------------------|--------|--------|----------|----------|
| Cost of revenue            | \$ 785 | \$ 721 | \$ 1,429 | \$ 1,595 |
| Product development        | 594    | 610    | 1,189    | 1,342    |
| Sales and marketing        | 562    | 598    | 1,026    | 1,368    |
| General and administrative | 585    | 697    | 1,157    | 1,356    |

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See notes to condensed consolidated financial statements

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|                                                        | <b>Three Months<br/>Ended<br/>December 31,</b> |             | <b>Six Months Ended<br/>December 31,</b> |             |
|--------------------------------------------------------|------------------------------------------------|-------------|------------------------------------------|-------------|
|                                                        | <b>2014</b>                                    | <b>2013</b> | <b>2014</b>                              | <b>2013</b> |
| Net loss                                               | \$ (5,477)                                     | \$ (44,029) | \$ (11,764)                              | \$ (44,968) |
| Other comprehensive loss                               |                                                |             |                                          |             |
| Unrealized gain (loss) on investments                  | 5                                              | (6)         | 13                                       |             |
| Foreign currency translation adjustment                | (18)                                           | 4           | (25)                                     | (71)        |
| Change in unrealized gain (loss) on interest rate swap | 28                                             | 93          | 254                                      | (44)        |
| Other comprehensive income (loss)                      | 15                                             | 91          | 242                                      | (115)       |
| Comprehensive loss                                     | \$ (5,462)                                     | \$ (43,938) | \$ (11,522)                              | \$ (45,083) |

See notes to condensed consolidated financial statements



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## QUINSTREET, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

|                                                                                 | Six Months Ended<br>December 31, |             |
|---------------------------------------------------------------------------------|----------------------------------|-------------|
|                                                                                 | 2014                             | 2013        |
| <b>Cash Flows from Operating Activities</b>                                     |                                  |             |
| Net loss                                                                        | \$ (11,764)                      | \$ (44,968) |
| Adjustments to reconcile net loss to net cash provided by operating activities: |                                  |             |
| Depreciation and amortization                                                   | 10,408                           | 13,344      |
| Provision for sales returns and doubtful accounts receivable                    | 470                              | (243)       |
| Write-off of bank loan upfront fees                                             | 328                              |             |
| Stock-based compensation                                                        | 4,801                            | 5,661       |
| Excess tax benefits from stock-based compensation                               | (51)                             | (309)       |
| Gain on sale of domain names                                                    | (3,158)                          |             |
| Other adjustments, net                                                          | 99                               | 538         |
| Changes in assets and liabilities, net of effects of acquisition:               |                                  |             |
| Accounts receivable                                                             | 394                              | 3,562       |
| Prepaid expenses and other assets                                               | (369)                            | (513)       |
| Other assets, noncurrent                                                        |                                  | (59)        |
| Deferred taxes                                                                  | 2                                | 40,393      |
| Accounts payable                                                                | 2,964                            | (196)       |
| Accrued liabilities                                                             | (3,449)                          | (5,861)     |
| Deferred revenue                                                                | 178                              | (638)       |
| Other liabilities, noncurrent                                                   | (253)                            | (370)       |
| Net cash provided by operating activities                                       | 600                              | 10,341      |
| <b>Cash Flows from Investing Activities</b>                                     |                                  |             |
| Capital expenditures                                                            | (2,285)                          | (4,179)     |
| Business acquisition                                                            |                                  | (875)       |
| Other intangibles                                                               |                                  | (2,692)     |
| Internal software development costs                                             | (933)                            | (1,204)     |
| Purchases of marketable securities                                              | (16,600)                         | (23,236)    |
| Proceeds from sales and maturities of marketable securities                     | 27,287                           | 21,345      |
| Proceeds from sale of domain names                                              | 3,158                            |             |
| Proceeds from sale of property and equipment                                    | 10                               |             |
| Net cash provided by (used in) investing activities                             | 10,637                           | (10,841)    |
| <b>Cash Flows from Financing Activities</b>                                     |                                  |             |

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|                                                                    |           |           |
|--------------------------------------------------------------------|-----------|-----------|
| Proceeds from exercise of common stock options                     | 1,300     | 1,927     |
| Principal payments on bank debt                                    | (7,500)   | (5,000)   |
| Payment of bank loan upfront fees                                  | (272)     |           |
| Principal payments on acquisition-related notes payable            | (444)     | (2,237)   |
| Excess tax benefits from stock-based compensation                  | 51        | 309       |
| Withholding taxes related to restricted stock net share settlement | (626)     | (1,328)   |
| Net cash used in financing activities                              | (7,491)   | (6,329)   |
| Effect of exchange rate changes on cash and cash equivalents       | 17        | (41)      |
| Net increase (decrease) in cash and cash equivalents               | 3,763     | (6,870)   |
| Cash and cash equivalents at beginning of period                   | 84,177    | 90,117    |
| Cash and cash equivalents at end of period                         | \$ 87,940 | \$ 83,247 |

**Supplemental Disclosure of Cash Flow Information**

|                        |       |       |
|------------------------|-------|-------|
| Cash paid for interest | 1,602 | 1,987 |
| Cash paid for taxes    | 660   | 1,221 |

See notes to condensed consolidated financial statements

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**QUINSTREET, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**1. The Company**

QuinStreet, Inc. (the Company) is a leader in performance marketing online. The Company was incorporated in California in April 1999 and reincorporated in Delaware in December 2009. The Company provides customer acquisition programs for clients in various industry verticals such as education and financial services. The corporate headquarters are located in Foster City, California, with additional offices throughout the United States, Brazil and India.

**2. Summary of Significant Accounting Policies**

**Basis of Presentation**

*Principles of Consolidation*

The condensed consolidated financial statements include the accounts of the Company and its subsidiaries. Intercompany balances and transactions have been eliminated in consolidation.

*Unaudited Interim Financial Information*

The accompanying condensed consolidated financial statements and the notes to the condensed consolidated financial statements as of December 31, 2014 and for the three and six months ended December 31, 2014 and 2013 are unaudited. These unaudited interim condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Accordingly, these interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2014, as filed with the SEC on September 12, 2014. The condensed consolidated balance sheet at June 30, 2014 included herein was derived from the audited financial statements as of that date, but does not include all disclosures, including notes, required by GAAP.

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, include all adjustments (consisting only of normal recurring adjustments) necessary for the fair statement of the Company's condensed consolidated balance sheet at December 31, 2014, its condensed consolidated statements of operations for the three and six months ended December 31, 2014 and 2013, its condensed consolidated statements of comprehensive loss for the three and six months ended December 31, 2014 and 2013, and its condensed consolidated statements of cash flows for the six months ended December 31, 2014 and 2013. The results of operations for the three and six months ended December 31, 2014 are not necessarily indicative of the results to be expected for the fiscal year ending June 30, 2015, or any other future period.

*Use of Estimates*

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the period. On an ongoing basis, management evaluates these estimates, judgments and assumptions, including those related to revenue recognition, stock-based compensation, goodwill, intangible assets, long-lived assets, contingencies, and income taxes. The Company bases these estimates on historical and anticipated results and trends and on various other assumptions that the Company believes are reasonable under the circumstances, including assumptions as to future events. These estimates form the basis for making judgments about the carrying values of assets and liabilities and recorded revenue and expenses that are not readily apparent from other sources. Actual results could differ from those estimates, and such differences could affect the results of operations reported in future periods.

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**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

***Accounting Policies***

The significant accounting policies are described in Note 2, Summary of Significant Accounting Policies, to the consolidated financial statements included in the Annual Report on Form 10-K for the fiscal year ended June 30, 2014. There have been no significant changes in the accounting policies subsequent to June 30, 2014.

***Concentrations of Credit Risk***

No client accounted for 10% or more of net revenue for the three or six months ended December 31, 2014 or for the same period in fiscal year 2014. No client accounted for 10% or more of net accounts receivable as of December 31, 2014 or June 30, 2014.

***Fair Value of Financial Instruments***

The Company's financial instruments consist principally of cash equivalents, marketable securities, accounts receivable, accounts payable, acquisition-related promissory notes, an interest rate swap, and a term loan. The fair value of the Company's cash equivalents is determined based on quoted prices in active markets for identical assets for its money market funds; and quoted prices for similar instruments in active markets for its U.S. municipal securities and certificates of deposits that mature within 90 days. The recorded values of the Company's accounts receivable and accounts payable approximate their current fair values due to the relatively short-term nature of these accounts. The fair values of acquisition-related promissory notes approximate their recorded amounts as the interest rates on similar financing arrangements available to the Company at December 31, 2014 approximate the interest rates implied when these acquisition-related promissory notes were originally issued and recorded. The fair value of the interest rate swap is based upon fair value quotes from the issuing bank and the Company assesses the quotes for reasonableness by comparing them to the present values of expected cash flows. The present value approach is based on observable market interest rate curves that are commensurate with the terms of the interest rate swap. The carrying value represents the fair value of the swap, as adjusted for any non-performance risk associated with the Company at December 31, 2014. The Company believes that the fair value of the term loan approximates its recorded amount at December 31, 2014 as the interest rate on the term loan is variable and is based on market interest rates and after consideration of default and credit risk.

***Recent Accounting Pronouncements***

In July 2013, the FASB issued a new accounting standard update on the financial presentation of unrecognized tax benefits. The new guidance provides that a liability related to an unrecognized tax benefit would be presented as reduction of a deferred tax asset for a net operating loss carryforward, a similar tax loss or a tax credit carryforward if such settlement is required or expected in the event the uncertain tax position is disallowed. The new guidance becomes effective July 1, 2015 for the Company and it should be applied prospectively to unrecognized tax benefits that exist at the effective date, although retrospective application is permitted. The Company does not believe that the adoption will have a material effect on the Company's consolidated financial statements.

In May 2014, the FASB issued a new accounting standard update on revenue from contracts with clients. The new guidance provides that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new guidance becomes effective July 1, 2017 for the Company. The Company is currently assessing the impact of this new guidance.

In June 2014, the FASB issued a new accounting standard update on accounting for share-based payments when the terms of an award provide that a performance target could be achieved after the requisite service period, which amends ASC 718, Compensation - Stock Compensation. The amendment provides guidance on the treatment of share-based payment awards with a specific performance target, requiring that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. The new guidance becomes effective for fiscal years beginning after December 15, 2015, and interim periods within those years, with early adoption permitted. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial statements.

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