inContact, Inc.
Form 10-Q
November 14, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the

Securities Exchange Act of 1934

For the Quarterly Period Ended September 30, 2014

Commission File No. 1-33762

inContact, Inc.

(Exact name of registrant as specified in its charter)

Delaware	87-0528557
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

7730 S. Union Park Avenue, Suite 500, Salt Lake City, UT 84047

(Address of principal executive offices and Zip Code)

(801) 320-3200

(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 x No ¨

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

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

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

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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date:

Class	Outstanding as of November 3, 2014
Common Stock, $0.0001 par value	60,994,316 shares

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ITEM NUMBER AND CAPTION

INCONTACT, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS—(Unaudited)

(in thousands, except per share data)

	September 30, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$31,085	$49,148
Restricted cash	81	81
Accounts and other receivables, net of allowance for uncollectible accounts of $1,652 and $2,203, respectively	23,267	18,682
Other current assets	7,516	4,360
Total current assets	61,949	72,271
Property and equipment, net	33,924	23,716
Intangible assets, net	26,103	3,971
Goodwill	39,432	6,563
Other assets	1,905	1,540
Total assets	$163,313	$108,061
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Trade accounts payable	$11,950	$9,696
Accrued liabilities	11,133	8,772
Accrued commissions	2,697	2,072
Current portion of deferred revenue	6,737	2,440
Current portion of debt and capital lease obligations	3,704	3,461
Total current liabilities	36,221	26,441
Long-term portion of debt and capital lease obligations	13,885	4,580
Deferred rent	37	487
Deferred tax liability	795	232
Deferred revenue	4,861	3,981
Total liabilities	55,799	35,721
Commitments and contingencies		
Stockholders' equity:		
Common stock, $0.0001 par value; 100,000 shares authorized; 60,981 and 55,346 shares issued and outstanding as of September 30, 2014 and December 31, 2013, respectively	6	6
Additional paid-in capital	207,626	167,422
Accumulated deficit	(100,118)	(95,088)

Total stockholders' equity	107,514	72,340
Total liabilities and stockholders' equity	$163,313	$108,061

See accompanying notes to condensed consolidated financial statements.

INCONTACT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS and COMPREHENSIVE LOSS

(Unaudited)

(in thousands, except per share data)

	Three months ended September 30, 2014	Three months ended September 30, 2013	Nine months ended September 30, 2014	Nine months ended September 30, 2013
Net revenue:				
Software	$26,286	$17,133	$70,493	$49,490
Network connectivity	17,909	15,106	51,867	45,477
Total net revenue	44,195	32,239	122,360	94,967
Costs of revenue:				
Software	12,018	7,078	30,486	19,857
Network connectivity	11,316	9,693	33,009	29,336
Total costs of revenue	23,334	16,771	63,495	49,193
Gross profit	20,861	15,468	58,865	45,774
Operating expenses:				
Selling and marketing	13,541	9,574	36,602	27,004
Research and development	6,316	3,043	15,554	8,778
General and administrative	7,500	5,550	20,525	15,924
Total operating expenses	27,357	18,167	72,681	51,706
Loss from operations	(6,496)	(2,699)	(13,816)	(5,932)
Other income (expense):				
Interest expense	(83)	(88)	(278)	(238)
Other income (expense)	1	1	(148)	(24)
Total other expense	(82)	(87)	(426)	(262)
Loss before income taxes	(6,578)	(2,786)	(14,242)	(6,194)
Income tax benefit (expense)	(106)	(41)	9,262	(90)
Net loss and comprehensive loss	$(6,684)	$(2,827)	$(4,980)	$(6,284)
Net loss per common share:				
Basic and diluted	$(0.11)	$(0.05)	$(0.09)	$(0.12)
Weighted average common shares outstanding:				
Basic and diluted	60,429	55,317	58,448	54,375

See accompanying notes to condensed consolidated financial statements.

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INCONTACT, INC.

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY—(Unaudited)

(in thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Treasury Stock Shares	Treasury Stock Amount	Accumulated Deficit	Total
Balance at December 31, 2013	55,346	$ 6	$ 167,422	-	$ -	$ (95,088)	$ 72,340
Common stock issued for options exercised	565	-	2,009	-	-	-	2,009
Common stock issued under the employee stock purchase plan	60	-	454	17	126	(14)	566
Common stock received for settlement of taxes and forfeited restricted stock	-	-	-	(69)	(162)	-	(162)
Issuance of common stock	3,822	-	31,951	-	-	-	31,951
Issuance of restricted stock	1,188	-	-	52	36	(36)	-
Stock-based compensation	-	-	5,790	-	-	-	5,790
Net loss	-	-	-	-	-	(4,980)	(4,980)
Balance at September 30, 2014	60,981	$ 6	$ 207,626	-	$ -	$ (100,118)	$ 107,514

See accompanying notes to condensed consolidated financial statements.

INCONTACT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(in thousands)

Cash flows from operating activities:	Nine months ended September 30, 2014			2013		
Net loss	$	(4,980	)	$	(6,284	)
Adjustments to reconcile net loss to net cash from operating activities:						
Depreciation of property and equipment		5,447			4,469	
Amortization of software development costs		4,300			3,475	
Amortization of intangible assets		2,316			270	
Amortization of note financing costs		21			14	
Interest accretion		3			5	
Stock-based compensation		5,790			2,961	
Loss on disposal of property and equipment		626			120	
Write-off of contingent liability		(146	)		-	
Deferred income taxes		(9,368	)		-	
Changes in operating assets and liabilities, net of business acquisitions:						
Accounts and other receivables, net		(3,843	)		(3,162	)
Other current assets		(1,793	)		(1,140	)
Other non-current assets		(333	)		(477	)
Trade accounts payable		1,875			1,137	
Accrued liabilities		(238	)		279	
Accrued commissions		(122	)		612	
Deferred rent		(145	)		134	

Deferred revenue		3,309			2,514	
Net cash provided by operating activities		2,719			4,927	
Cash flows from investing activities:						
Payments made for deposits		(32	)		(12	)
Acquisition of assets		-			(2,746	)
Acquisition of a business, net of cash acquired		(11,992	)		(2,700	)
Capitalized software development costs		(8,052	)		(4,583	)
Purchases of property and equipment		(10,920	)		(3,365	)
Net cash used in investing activities		(30,996	)		(13,406	)
Cash flows from financing activities:						
Proceeds from exercise of options		2,009			6,475	
Proceeds from sale of stock under employee stock purchase plan		566			326	
Borrowings under term loans		1,000			4,000	
Payment of debt financing fees		(45	)		(43	)
Principal payments under debt and capital lease obligations		(3,154	)		(2,504	)
Purchase of treasury stock		(162	)		-	
Borrowings under revolving credit agreement		10,000			-	
Payments under the revolving credit agreement		-			(1,000	)
Net cash provided by financing activities		10,214			7,254	
Net decrease in cash and cash equivalents		(18,063	)		(1,225	)
Cash and cash equivalents at beginning of period		49,148			48,836	
Cash and cash equivalents at end of the period	$	31,085		$	47,611	

Supplemental schedule of non-cash investing and financing activities:				
Payments due for property and equipment included in trade accounts payable	$	640	$	227
Property and equipment financed through capital leases	$	1,702	$	-
Common stock received for settlement of receivables and taxes	$	-	$	2,937
Issuance of common stock for acquisition of a business	$	31,951	$	2,910
Consideration for acquisition of a business included in accrued liabilities likely to be paid in cash based on the final calculation of net closing current assets	$	1,252	$	-
Contingent consideration included in accrued liabilities	$	-	$	145

See accompanying notes to condensed consolidated financial statements.

INCONTACT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. ORGANIZATION AND BASIS OF PRESENTATION

Organization

inContact, Inc. (“inContact,” “we,” “us,” “our,” or the “Company”) is incorporated in the state of Delaware. We provide cloud contact center software solutions through our inContact® portfolio, an advanced contact handling and performance management software application. Our services provide a variety of connectivity options for carrying inbound calls to our inContact portfolio or linking agents to our inContact applications. We provide customers the ability to monitor agent effectiveness through our user survey tools and the ability to efficiently monitor their agent needs. We are also an aggregator and provider of network connectivity services (formerly telecommunications). We contract with a number of third party providers for the right to resell the various network connectivity services and products they provide, and then offer all of these services to our customers. These services and products allow customers to buy only the network connectivity services they need, combine those services in a customized enhanced contact center package, receive one bill for those services, and call a single point of contact if a service problem or billing issue arises.

Basis of Presentation

These unaudited condensed consolidated financial statements of inContact and its subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) and the rules and regulations of the United States Securities and Exchange Commission (“SEC”). Such rules and regulations allow the omission of certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP, so long as the statements are not misleading. In the opinion of management, these financial statements and accompanying notes contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly the financial position and results of operations for the periods presented herein. These condensed consolidated financial statements should be read in conjunction with the consolidated audited financial statements and notes thereto contained in the Annual Report on Form 10-K/A for the year ended December 31, 2013, filed with the SEC on November 14, 2014. The results of operations for the three and nine month periods ended September 30, 2014 are not necessarily indicative of the results to be expected for the year ending December 31, 2014. Our significant accounting policies are set forth in Note 1 to the Consolidated Financial Statements in the 2013 Annual Report on Form 10-K/A and changes, if any, are included below.

Revenue Recognition

Revenue is recognized when all of the following four criteria are met: (1) persuasive evidence of an arrangement exists, (2) the fee is fixed or determinable, (3) collection is reasonably assured, and (4) delivery has occurred or services have been rendered. Determining whether and when some of these criteria have been satisfied often involves assumptions and judgments that can have a significant impact on the timing and amount of revenue we report.

Our revenue is reported and recognized based on the type of services provided to the customer as follows:

Software Revenue. Software revenue includes two main sources of revenue:

(1) Software delivery and support of our inContact portfolio products that are provided on a monthly subscription basis and associated professional services. Because our customers purchasing software and support services on a monthly recurring basis do not have the right to take possession of the software, we consider these arrangements to be service contracts and are not within the scope of Industry Topic 985, Software. We generally bill monthly recurring subscription charges in arrears and recognize these charges in the period in which they are earned. In addition to the monthly recurring revenue, revenue is also received on a non-recurring basis for professional services or on a recurring basis related to improving a customer’s contact center efficiency and effectiveness as it relates to utilization of the inContact portfolio.

For subscription service contracts with multiple elements (hosted software, training, installation and long distance services), we follow the guidance provided in Accounting Standards Codification (“ASC”) 605-25, Revenue Recognition for Multiple Element Arrangements. In addition to the monthly recurring subscription revenue, we also derive revenue on a non-recurring basis for professional services included in implementing or improving a customer’s inContact portfolio experience. Because our professional services, such as training and implementation, are not considered to have standalone value, we defer revenue for upfront fees received for professional services in multiple element arrangements and recognize such fees as revenue over the estimated life of the customer. Fees for network connectivity services in multiple element arrangements within the inContact portfolio are based on usage and recognize revenue in the same manner as fees for telecommunication services discussed in the “Network Connectivity Services Revenue” below.

(2) Perpetual product and services revenues are primarily derived from the sale of software licenses of products within our inContact portfolio. For software license arrangements that do not require significant modification or customization of the underlying software, revenue is recognized when all four criteria listed above are met.

Many of our customers purchase a combination of software, service, hardware, post contract customer support ("PCS") and hosting. For software and software related multiple element arrangements that fall within the scope of the software revenue guidance in Topic 985, Software, we allocate revenue to the delivered elements of the arrangement using the residual method, whereby revenue is allocated to the undelivered elements based on vendor-specific objective evidence of fair value ("VSOE") of the undelivered elements with the remaining arrangement fee allocated to the delivered elements and is recognized as revenue assuming all other revenue recognition criteria are met. If we are unable to establish VSOE for the undelivered elements of the arrangement, including PCS, revenue recognition is deferred for the entire arrangement until all elements of the arrangement are delivered. PCS provided to our customers includes technical software support services and unspecified software upgrades to customers on a when-and-if available basis. PCS revenue is recognized ratably over the term of the maintenance period, which is typically 15 months. When PCS is included within a multiple element arrangement, we utilize the bell-shaped curve approach to establish VSOE for the PCS. Under the bell-shaped curve approach of establishing VSOE, we perform a VSOE compliance test on a quarterly basis to ensure that a substantial majority of our actual PCS renewals are within a sufficiently narrow range.

Product revenue derived from shipments to customers who purchase our products for resale and is generally recognized when such products are shipped (on a "sell-in" basis). We have historically experienced insignificant product returns from resellers, and our payment terms for these customers are similar to those granted to our end-users. If a reseller develops a pattern of payment delinquency, or seeks payment terms longer than generally accepted, we defer the revenue until the receipt of cash. Our arrangements with resellers are periodically reviewed as our business and products change.

Through the quarter ended September 30, 2014, software revenue also includes the quarterly minimum purchase commitments from a related party reseller (Note 13).

Network Connectivity Service Revenue. Network Connectivity Services revenue is derived from network connectivity, such as dedicated transport, switched long distance and data services. These services are provided over our network or through third party network connectivity providers. Our network is the backbone of our subscription services portfolio and allows us to provide the all-in-one inContact solution. Revenue for the network connectivity usage is derived based on customer specific rate plans and the customer's call usage and is recognized in the period the call is initiated. Customers are also billed monthly charges in arrears and revenue is recognized for such charges over the billing period. If the billing period spans more than one month, earned but unbilled revenues are recognized as revenue for incurred usage to date.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers." The core principle behind ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for delivering those goods and services. This model involves a five-step process that includes identifying the contract with the customer, identifying the performance obligations in the contract, determining the transaction price, allocating the transaction prices to the performance obligations in the contract and recognizing revenue when (or as) the entity satisfies the performance obligations. The guidance in the ASU supersedes existing revenue recognition guidance and is effective for annual reporting periods beginning after December 15, 2016 with early application not permitted. The ASU allows two methods of adoption; a full retrospective approach where three years of financial information are presented in accordance with the new standard, and a modified retrospective approach where the ASU is applied to the most current period presented in the financial statements. We are currently evaluating the impact of adopting the new revenue standard on our consolidated financial statements.

In April 2014, the FASB issued ASU No. 2014-14, “Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity,” which changes the criteria for reporting discontinued operations and requires additional disclosures about discontinued operations. Under the new guidance, only disposals representing a strategic shift in operations that have, or will have, a major effect on the organization’s operations and financial results should be presented as discontinued operations. Additionally, the guidance requires expanded disclosures about discontinued operations that will provide financial statement users with more information about the assets, liabilities, income, and expenses of discontinued operations. The amendments in ASU No. 2014-08 will be applied prospectively to annual periods beginning on or after December 15, 2014, and interim periods within those years, with early adoption permitted. We do not expect this guidance to have any effect on our financial statements.

In August 2014, the FASB issued ASU No. 2014-15, “Disclosure of Uncertainties about an Entity’s ability to Continue as a Going Concern”, which amended guidance related to disclosure of uncertainties about an entity’s ability to continue as a going concern, with an effective date of December 31, 2016. The new guidance requires management of all entities to evaluate whether there is substantial doubt about the entity's ability to continue as a going concern and, as necessary, to provide related footnote disclosures. We do not expect this guidance to have any effect on our financial statements.

NOTE 2. RESTATEMENT OF PREVIOUSLY ISSUED FINANCIAL STATEMENTS

Subsequent to the issuance of the Company's second quarter 2014 Condensed Consolidated Financial Statements, we determined that errors existed in the Company's previously issued Condensed Consolidated Financial Statements. As a result, the accompanying Condensed Consolidated Financial Statements have been restated to correct for such errors, as described below.

Management's decision to restate the aforementioned financial statements was made as a result of the identification of errors related to the calculation and assessment of state sales tax for certain of our products and services and the appropriate accounting for the related state sales tax obligations which cannot now be collected from customers due to the amount time that has lapsed.

The principal effect of the restatement adjustments is to increase net loss by $311,000 and $829,000 (including increasing General and Administrative expense by the same amount) for the three and nine months ended September 30, 2013, respectively, and increase accrued liabilities by the corresponding amount.

The impact of the restatement adjustments on specific line items on the Company's previously issued Condensed Consolidated Statements of Operations and Comprehensive Loss and Cash Flows for the three and nine months ended September 30, 2013 are presented below (in thousands, except per share amounts):

	Condensed Consolidated Statement of Operations and Comprehensive Loss for the three months ended September 30, 2013		
	As Previously Reported	Adjustments	As Restated
General and administrative	$ 5,239	$ 311	$ 5,550
Total operating expenses	17,856	311	18,167
Loss from operations	(2,388)	(311)	(2,699)
Loss before income taxes	(2,475)	(311)	(2,786)
Net loss and comprehensive loss	(2,516)	(311)	(2,827)
Net loss per common share:			
Basic and diluted	$ (0.05)	$ -	$ (0.05)

	Condensed Consolidated Statement of Operations and Comprehensive Income for the nine months ended September 30, 2013		
	As Previously Reported	Adjustments	As Restated
General and administrative	$ 15,095	$ 829	$ 15,924
Total operating expenses	50,877	829	51,706
Loss from operations	(5,103)	(829)	(5,932)
Loss before income taxes	(5,365)	(829)	(6,194)
Net loss and comprehensive loss	(5,455)	(829)	(6,284)
Net loss per common share:			
Basic and diluted	$ (0.10)	$ (0.02)	$ (0.12)

	Consolidated Statement of Cash Flows for the nine months ended September 30, 2013		
	As Previously Reported	Adjustments	As Restated
Net loss	$ (5,455)	$ (829)	$ (6,284)
Changes in operating assets and liabilities:			
Increase in accrued liabilities	(550)	829	279

The Company believes that the effects of these errors are not material to the previously issued Condensed Consolidated Financial Statements.

NOTE 3. ASSET ACQUISITION

In March 2013, we acquired technology for $1.9 million in cash, which we used to add mobile and social features in our existing applications. In April and June 2013, development earnout measures were achieved resulting in additional payments totaling $800,000. The value of the assets acquired was recorded as in process technology and was included in internal use software. In

December 2013, we determined that $545,000 of the acquired technology would not be utilized in the foreseeable future and therefore was disposed.

NOTE 4. BASIC AND DILUTED NET LOSS PER COMMON SHARE

Basic earnings per common share is computed by dividing the net income or loss applicable to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share is computed by dividing the net income or loss by the sum of the weighted-average number of common shares outstanding plus the weighted average common stock equivalents, which would have been outstanding if the potentially dilutive securities had been issued. Potentially dilutive securities include outstanding options, warrants and restricted stock units. The dilutive effect of potentially dilutive securities is reflected in diluted earnings per common share by application of the treasury method.

As a result of incurring a net loss for the three and nine months ended September 30, 2014 and 2013, no potentially dilutive securities are included in the calculation of diluted earnings per share because such effect would be anti-dilutive. We had potentially dilutive securities representing approximately 4.5 million and 3.4 million shares of common stock at September 30, 2014 and 2013, respectively.

NOTE 5. FAIR VALUE OF FINANCIAL INSTRUMENTS

The accounting guidance for fair value measurements defines fair value, establishes a market-based framework or hierarchy for measuring fair value and expands disclosures about fair value measurements. The guidance is applicable whenever assets and liabilities are measured and included in the financial statements at fair value. The fair value of a financial instrument is the amount that could be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Financial assets are marked to bid prices and financial liabilities are marked to offer prices. Fair value measurements do not include transaction costs. The fair value hierarchy prioritizes the quality and reliability of the information used to determine fair values. Categorization within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The fair value hierarchy is defined into the following three categories:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

Fair Value of Other Financial Instruments

The carrying amounts reported in the accompanying Condensed Consolidated Balance Sheets for cash and cash equivalents, accounts and other receivables, and trade accounts payable approximate fair value because of the immediate or short-term maturities of these financial instruments and are considered to be classified within Level 2 of the fair value hierarchy, except for cash and cash equivalents which is Level 1. The fair values of the promissory notes payable, term loans and revolving line of credit were computed using a discounted cash flow model using estimated market rates adjusted for our credit risk as of September 30, 2014 and December 31, 2013. We consider the input related to our credit risk to be within Level 3 of the fair value hierarchy due to the limited number of our debt holders and our inability to observe current market information. We estimated our current credit risk as of September 30, 2014 and December 31, 2013 based on recent transactions with our creditors. The carrying value and estimated fair value of our promissory notes payable and term loans are as follows (in thousands):

	September 30, 2014		December 31, 2013	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Promissory notes	$69	$ 69	$694	$ 694
Term loans	$6,115	$ 6,115	$6,223	$ 6,223
Revolving credit	$10,000	$ 10,000	$-	$ -

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NOTE 6. ACQUISITIONS

Uptivity Acquisition

On May 6, 2014, we acquired 100% of the outstanding shares of CallCopy, Inc., a Delaware corporation doing business as Uptivity ("Uptivity"). Uptivity provides a complete mid-market workforce optimization suite of software products and services to call centers comprised of speech and desktop analytics, agent coaching, call and desktop recording, as well as quality, performance, workforce management and satisfaction surveys. inContact acquired Uptivity for an aggregate purchase price of $49.1 million of primarily cash and stock. The purchase consideration was paid with cash in the amount of $12.1 million, estimated fair market value of vested stock options converted to cash of $1.9 million, 3,821,933 shares of the Company's common stock valued at approximately $32.0 million and $3.1 million likely to be paid in cash based on the final calculation of net closing current assets, of which $1.9 million was paid during the third quarter of 2014. An additional 434,311 shares of restricted common stock were issued, but not included in the purchase consideration because the shares are subject to repurchase rights which will lapse as services are provided over a three year period. The acquisition of Uptivity was accounted for under the purchase method of accounting in accordance with ASC 805, Business Combinations. Under the purchase method of accounting, the total purchase price is allocated to the preliminary tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values, as determined by management. The total purchase price was allocated using the information currently available. The purchase price allocation for the Uptivity acquisition will be finalized in calendar year 2015. As a result, we may continue to adjust the preliminary estimated purchase price allocation after obtaining more information regarding asset valuations, liabilities assumed, and revision of preliminary estimates. The following is the total preliminary purchase price allocation of the estimated purchase consideration based on available information as of September 30, 2014 (in thousands):

	Amount
Assets acquired:	
Cash	$3,894
Accounts receivable	742
Other current assets	1,363
Property, plant and equipment and other assets	584
Intangible assets	24,448
Goodwill	32,870
Total assets acquired	63,901
Liabilities assumed:	
Trade accounts payable	1,124
Accrued liabilities	1,934
Current portion of deferred revenue	1,516
Long-term portion of deferred revenue	353
Deferred tax liability	9,884
Total liabilities assumed	14,811
Net assets acquired	$49,090

In connection with the acquisition, we incurred professional fees of $934,000, including transaction costs such as legal and valuation services, which were expensed as incurred. These costs are included within general and administrative expenses in the Condensed Consolidated Statements of Operations. The premium paid over the fair value of the net assets acquired in the purchase, or goodwill, represents future economic benefits expected to arise from synergies from combining operations and assembled workforce acquired. All of the goodwill was assigned to the software segment. The entire amount allocated to goodwill is not expected to be deductible for tax purposes.

Intangible assets acquired resulting from the acquisition include customer relationships, which are amortized on a double-declining basis, technologies, which are amortized on a straight-line basis and in-process research and development which has an initial indefinite life and is expected to be amortized once technical feasibility is established. The fair values of the intangible assets were determined primarily using the income approach and the discount rates range from 17.0% to 20.6%. The following sets forth the intangible assets purchased as part of the Uptivity acquisition and their economic preliminary estimated useful life as of September 30, 2014 (in thousands, except useful life):

	Amount	Economic Useful Life (in years)
Customer relationships	$11,460	8
Trade name and trademarks	1,942	5
Technology	7,686	7
In-process research and development	3,360	Indefinite
Total intangible assets	$24,448	

The Company recorded a deferred tax benefit of $9.4 million for the nine months ended September 30, 2014. The tax benefit related to recording a deferred tax liability upon acquisition of Uptivity related to a reduction of carrying value of deferred revenue and acquisition of intangibles for which no tax benefit will be derived. The reduction of carrying value resulted in a partial reversal of the deferred tax asset valuation allowance upon consolidation.

In the quarter ended September 30, 2014, our consolidated financial statements include approximately $4.4 million and $2.5 million of net revenue and net loss, respectively, related to the operations of Uptivity. In the nine months ended September 30, 2014, our consolidated financial statements include approximately $7.3 million and $4.3 million of net revenue and net loss, respectively, related to the operations of Uptivity. The following table presents our unaudited pro forma results of operations of the Company and Uptivity as if the companies had been combined as of January 1, 2013, and includes pro forma adjustments related to the fair value of deferred revenue, amortization of acquired intangible assets and share-based compensation expense. Direct and incremental transaction costs are excluded from the period ended September 30, 2014 pro forma condensed combined financial information presented below, and included in the period ended September 30, 2013 pro forma condensed combined financial information presented below. The tax benefit of $9.4 million that resulted from the acquisition is recorded in the nine months ended September 30, 2013 pro-forma period.

	Three months ended	Nine months ended
		September 30, 2014

	September 30, 2014			
	As Reported	Proforma	As Reported	Proforma
Net revenue	$44,195	$44,170	$122,360	$129,469
Net loss	(6,684)	(6,470)	(4,980)	(16,912)
Basic and diluted net loss per common share	$(0.11)	$(0.11)	$(0.09)	$(0.29)

	Three months ended		Nine months ended	
	September 30, 2013		September 30, 2013	
	As Reported	Proforma	As Reported	Proforma
Net revenue	$32,239	$37,055	$94,967	$106,683
Net loss	(2,827)	(6,274)	(6,284)	(9,895)
Basic and diluted net loss per common share	$(0.05)	$(0.11)	$(0.12)	$(0.18)

The unaudited pro forma information set forth above is for informational purposes only. The pro forma information should not be considered indicative of actual results that would have been achieved had Uptivity been acquired at the beginning of 2013 or of results that may be obtained in any future period.

Transcend Acquisition

In December 2012, we entered into an agreement with Transcend Products LLC ("Transcend") pertaining to the potential acquisition of Transcend to provide enhanced functionality for our existing service offerings. The option to purchase Transcend was exercised and the purchase closed in July 2013 for $2.7 million in cash and 376,459 shares of our common stock valued at $2.9 million, which was discounted from $3.0 million in the purchase agreement for the lack of marketability. Furthermore, if the acquisition generates certain levels of revenue during the two-year period beginning in August 2013, we will pay to Transcend an additional earnout payment of $1.0 million in cash or shares of our common stock. As of the date of acquisition, this contingent liability has been recorded in accrued liabilities at its fair market value of $146,000 and was included as part of the purchase consideration. During the third quarter of 2014, the Company determined that fair market value of this contingent liability decreased to zero and therefore was eliminated. The Company recorded a benefit of $146,000, relating to the remeasurement of the fair value of the contingent liability which was included in software cost of revenue in the Condensed Consolidated and Statements of Operations.

The purchase price allocations for our acquisition of Transcend Products were prepared by the Company's management utilizing a valuation report, which was prepared in accordance with the provisions of ASC 805 Business Combination, and other tools available to the Company, including conversations with Transcend's management and projections of revenues and expenses. The fair values of the intangible assets were determined primarily using the income approach and the discount rates range from 13.4% to 16.4%. The total purchase consideration, which includes the contingent consideration liability above, was allocated as follows (in thousands):

	July 2, 2013
Property and equipment, net	$29
Intangible assets, net	3,249
Goodwill	2,477
Total assets acquired	$5,755

In connection with the acquisition, we incurred professional fees of $23,000, including transaction costs such as legal and valuation services, which were expensed as incurred. These costs are included within general and administrative expenses in the Condensed Consolidated Statements of Operations.

The premium paid over the fair value of the net assets acquired in the purchase, or goodwill, was primarily attributed to buyer synergies and assembled workforce. All of the goodwill was assigned to the software segment.

Intangible assets acquired resulting from the acquisition include customer relationships, patents and technology and are amortized on a straight-line basis. The following sets forth the intangible assets purchased as part of the Transcend acquisition and their economic useful life at the date of acquisition (in thousands, except useful life):

	Intangible Assets	Economic Useful Life (in years)
Customer relationships	$ 168	3.5
Patents	2,168	10.0

Technology	913	5.0
Total intangible assets	$ 3,249	

NOTE 7. INTANGIBLE ASSETS

Intangible assets consisted of the following (in thousands):

	September 30, 2014			December 31, 2013		
	Gross Assets	Accumulated Amortization	Intangible Assets, Net	Gross Assets	Accumulated Amortization	Intangible Assets, Net
Customer lists acquired	$28,123	$ (17,626)	$ 10,497	$16,663	$ (16,354)	$ 309
Technology and patents	21,094	(11,169)	9,925	13,312	(10,347)	2,965
Trade names and trademarks	3,136	(773)	2,363	1,194	(551)	643
In-process R&D	3,264	-	3,264	-	-	-
Domain name	54	-	54	54	-	54
Total intangible assets	$55,671	$ (29,568)	$ 26,103	$31,223	$ (27,252)	$ 3,971

Amortization expense was $2.3 million and $270,000 during the nine months ended September 2014 and 2013, respectively

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Based on the recorded intangibles at September 30, 2014, estimated amortization expense is expected to be $1.2 million during the remainder of 2014, $4.5 million in 2015, $3.8 million in 2016, $3.2 million in 2017, $2.9 million in 2018 and $7.2 million thereafter.

NOTE 8. ACCRUED LIABILITIES

Accrued liabilities consisted of the following (in thousands):