VIEWPOINT CORP/NY/
Form 10-Q
August 14, 2002

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# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 10-Q

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended June 30, 2002**

**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: 0-27168**

# VIEWPOINT CORPORATION

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Delaware** | **95-4102687** |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

**498 Seventh Avenue, Suite 1810, New York, NY 10018**
(Address of principal executive offices and zip code)

**(212) 201-0800**
(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 reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

As of August 2, 2002, 40,972,738 shares of $0.001 par value common stock were outstanding.

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## PART I FINANCIAL INFORMATION

### Item 1. Consolidated Financial Statements

**VIEWPOINT CORPORATION**
**CONSOLIDATED BALANCE SHEETS**
**(in thousands, except per share data)**
**(Unaudited)**

| | June 30, 2002 | December 31, 2001 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $8,247 | $8,345 |
| Marketable securities | 3,848 | 7,068 |
| Accounts receivable, net | 4,744 | 4,096 |
| Notes receivable, net | 750 | 750 |
| Prepaid expenses and other current assets | 491 | 836 |
| Current assets related to discontinued operations | | 141 |
| Total current assets | 18,080 | 21,236 |
| Property and equipment, net | 4,205 | 4,662 |
| Goodwill, net | 31,276 | 33,042 |
| Intangible assets, net | 144 | 2,361 |
| Loans to officers | 609 | 595 |
| Other assets | 4 | 21 |

| | | |
|---|---|---|
| Total assets | $54,318 | $61,917 |

**LIABILITIES AND STOCKHOLDERS EQUITY**

| | | |
|---|---|---|
| Current liabilities: | | |
| Accounts payable | $1,308 | $1,314 |
| Accrued expenses | 1,052 | 1,304 |
| Due to related parties, net | 3,099 | 4,764 |
| Deferred revenues | 822 | 907 |
| Accrued incentive compensation | 545 | 545 |
| Current liabilities related to discontinued operations | 240 | 346 |
| Total current liabilities | 7,066 | 9,180 |
| Stockholders equity: | | |
| Preferred stock, $.001 par value; 5,000 shares authorized-no shares issued and outstanding at June 30, 2002 and December 31, 2001 | | |
| Common stock, $.001 par value; 75,000 shares authorized 41,130 shares issued and 40,970 shares outstanding at June 30, 2002, and 39,620 shares issued and 39,460 shares outstanding at December 31, 2001 | 41 | 40 |
| Paid-in capital | 268,127 | 263,157 |
| Deferred compensation | (7,218) | (11,279) |
| Treasury stock at cost; 160 shares at June 30, 2002 and December 31, 2001 | (1,015) | (1,015) |
| Accumulated other comprehensive income | | |

| | | |
|---|---|---|
| | 77 | 18 |
| Accumulated deficit | (212,760) | (198,184) |
| Total stockholders equity | 47,252 | 52,737 |
| Total liabilities and stockholders equity | $54,318 | $61,917 |

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

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**VIEWPOINT CORPORATION**
**CONSOLIDATED STATEMENTS OF OPERATIONS**
**(in thousands, except per share data)**
**(Unaudited)**

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | **2002** | **2001** | **2002** | **2001** |
| Revenues: | | | | |
| Licenses | $3,862 | $1,780 | $7,401 | $3,688 |
| Services | 1,442 | 971 | 2,761 | 1,854 |
| Total revenues | 5,304 | 2,751 | 10,162 | 5,542 |
| Cost of revenues: | | | | |
| Licenses | 136 | 67 | 245 | 163 |
| Services | 914 | 568 | 1,822 | 1,378 |

| | | | | |
|---|---|---|---|---|
| Total cost of revenues | 1,050 | 635 | 2,067 | 1,541 |
| Gross profit | 4,254 | 2,116 | 8,095 | 4,001 |
| Operating expenses: | | | | |
| Sales and marketing (including non-cash stock-based compensation charges totaling $746 and $681 for the three months ended June 30, 2002 and 2001, respectively and $1,790 and $1,277 for the six months ended June 30, 2002 and 2001, respectively) | 3,750 | 5,356 | 7,651 | 10,531 |
| Research and development (including non-cash stock-based compensation charges totaling $160 and $745 for the three months ended June 30, 2002 and 2001, respectively and $355 and $1,485 for the six months ended June 30, 2002 and 2001, respectively) | 1,369 | 2,146 | 2,695 | 4,594 |
| General and administrative (including non-cash stock-based compensation charges totaling $414 and $388 for the three months ended June 30, 2002 and 2001, respectively and $828 and $795 for the six months ended June 30, 2002 and 2001, respectively) | 2,394 | 2,716 | 4,599 | 4,899 |
| Depreciation | 472 | 440 | 970 | 855 |
| Amortization of intangible assets | 2 | 831 | 663 | 1,662 |
| Amortization of goodwill | | 3,452 | | 6,758 |
| Impairment of goodwill and other intangible assets | | | 6,275 | |

| | | | | |
|---|---|---|---|---|
| Total operating expenses | 7,987 | 14,941 | 22,853 | 29,299 |
| Loss from operations | (3,733) | (12,825) | (14,758) | (25,298) |
| Other income | 48 | 293 | 89 | 717 |
| Net loss from continuing operations | (3,685) | (12,532) | (14,669) | (24,581) |
| Adjustment to net loss on disposal of discontinued operations | 93 | 730 | 93 | 730 |
| Net loss | $(3,592) | $(11,802) | $(14,576) | $(23,851) |

Basic and diluted net loss per common share:

| | | | | |
|---|---|---|---|---|
| Net loss per common share from continuing operations | $(0.09) | $(0.33) | $(0.36) | $(0.64) |
| Net income per common share from discontinued operations | | 0.02 | | 0.02 |
| Net loss per common share | $(0.09) | $(0.31) | $(0.36) | $(0.62) |
| Weighted average number of shares outstanding basic and diluted | 40,706 | 38,457 | 40,519 | 38,223 |

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

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**VIEWPOINT CORPORATION**
**CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(in thousands)**
**(Unaudited)**

| | Six Months Ended June 30, 2002 | Six Months Ended June 30, 2001 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net loss | $(14,576) | $(23,851) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Adjustment to net loss on disposal of discontinued operations | (93) | (730) |
| Non-cash stock-based compensation charges | 2,973 | 3,557 |
| Depreciation and amortization | 1,633 | 9,275 |
| Provision for bad debt | 126 | 150 |
| Impairment of goodwill and other intangible assets | 6,275 | |
| Reserve of notes receivable | | (665) |
| Loss on sale and disposal of equipment | 45 | |
| Accrued interest income | (14) | |
| Changes in operating assets and liabilities, net of acquisitions: | | |
| Accounts receivable | (774) | (579) |
| Prepaid expenses and other assets | 362 | (408) |
| Accounts payable | (6) | (509) |
| Accrued expenses | (252) | 1,168 |
| Due to/from related parties | 160 | 225 |
| Deferred revenues | (85) | (49) |
| Net cash provided by discontinued operations | | |

128 5,977

Net cash used in operating activities
(4,098) (6,439)
Cash flows from investing activities:

Purchases of property and equipment
(558) (660)
Purchases of patents and trademarks
(27) (39)
Purchases of marketable securities
(3,520) (19,232)
Proceeds from sales and maturities of marketable securities
6,800 18,200

Net cash provided by (used in) investing activities
2,695 (1,731)
Cash flows from financing activities:

Issuance of loans to officers
(575)
Proceeds from exercise of stock options
1,306 1,504

Net cash provided by financing activities
1,306 929
Effect of exchange rate changes on cash and cash equivalents
(1) (7)

| | | |
|---|---|---|
| Net decrease in cash and cash equivalents | (98) | (7,248) |
| Cash and cash equivalents at beginning of period | 8,345 | 13,320 |
| Cash and cash equivalents at end of period | $8,247 | $6,072 |

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

**VIEWPOINT CORPORATION**
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. Summary of Significant Accounting Policies**

**Basis of Presentation**

The unaudited consolidated financial statements at June 30, 2002 and for the three and six months ended June 30, 2002 and 2001 have been prepared in accordance with accounting principles generally accepted in the United States of America. The interim financial information is unaudited, but reflects all adjustments (consisting only of normal recurring accruals) that are, in the opinion of management, necessary for a fair presentation of Viewpoint Corporation s ( Viewpoint or the Company ) financial position and operating results for the interim periods.

These unaudited consolidated financial statements have been prepared in accordance with the instructions for Form 10-Q and, therefore, do not include all information and notes normally provided in annual financial statements. As a result, these unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto, together with management s discussion and analysis of financial condition and results of operations, contained in Viewpoint s annual report on Form 10-K for the fiscal year ended December 31, 2001. The results of operations for the three and six months ended June 30, 2002 are not necessarily indicative of the results to be expected for the fiscal year ending December 31, 2002 or any other future periods.

Certain reclassifications have been made to the 2001 consolidated financial statements to conform to the 2002 presentation.

**Revenue Recognition**

Revenue recognition rules for software companies are very complex. We follow very specific and detailed guidelines in measuring revenue; however, certain judgments affect the application of our revenue policy.

The Company recognizes revenue in accordance with Statement of Position ( SOP ) 97-2, Software Revenue Recognition, as amended, and Staff Accounting Bulletin ( SAB ) No. 101 Revenue Recognition in Financial Statements.

Viewpoint generates revenues through two sources: (a) software licenses and (b) services. License revenues are generated from licensing the rights to use our products directly to end-users and indirectly through value added resellers ( VARs ). Service revenues are generated from fee-based professional services, sales of customer support services (maintenance contracts), and training services performed for customers that license our products.

License revenue includes sales of perpetual and term-based licenses for broadcasting digital content in the Viewpoint format, and limited licenses for its digital content library. License revenue is recognized over the term of the license in a term-based broadcast license model and up-front in a perpetual broadcast license model, providing that no significant vendor obligations remain and the resulting receivable is deemed collectible by management.

Fee-based professional services are performed on a time-and-material basis or on a fixed-fee basis, under separate service arrangements. Revenues related to these services are recognized on a percentage-of-completion basis in accordance with the provisions of SOP 81-1 Accounting For Performance of Construction-Type and Certain Production-Type Contracts. Percentage-of-completion for service contracts is measured principally by the percentage of costs incurred and accrued to date for each contract to the estimated total cost for each contract at completion. Revenues from customer support services are recognized ratably over the term of the contract. Revenues from training services are recognized as services are performed.

Standard terms for license agreements call for payment within 90 days. Probability of collection is based upon the assessment of the customer s financial condition through the review of their current financial statements or credit

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**VIEWPOINT CORPORATION**
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)**

reports. For follow-on sales to existing customers, prior payment history is also used to evaluate probability of collection. Our agreements with customers do not contain product return rights.

Fees from licenses sold together with fee-based professional services are generally recognized upon delivery of the software, provided that the payment of the license fees are not dependent upon the performance of the services, and the services are not essential to the functionality of the licensed software. If the services are essential to the functionality of the software or payment of the license fees are dependent upon the performance of the services, both the software license and service fees are recognized under the percentage-of-completion method of contract accounting.

If the fee is not fixed or determinable, revenue is recognized as payments become due from the customer. If a nonstandard acceptance period is required, revenues are recognized upon the earlier of customer acceptance or the expiration of the acceptance period.

The Company periodically enters into nonmonetary arrangements whereby the Company s licenses or services are exchanged for services of its customers. Nonmonetary revenue is recognized at the estimated fair value of the services received. Generally, nonmonetary revenues equal nonmonetary expenses; however, due to timing, nonmonetary accounts receivable and accounts payable may result.

**Recent Accounting Pronouncements**

In July 2001, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 143, Accounting for Asset Retirement Obligations. The statement requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred. The statement is effective for fiscal years beginning after June 15, 2002. The adoption of SFAS No. 143 is not expected to have a material impact on the Company s financial statements.

In July 2002, the FASB issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities. This Statement addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies EITF Issue No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring). This Statement requires recognition of a liability for a cost associated with an exit or disposal activity when the liability is incurred, as opposed to when the entity commits to an exit plan under EITF No. 94-3. SFAS No. 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002. The adoption of SFAS No. 146 is not expected to have a material impact on the Company s financial statements.

**2. Net Loss Per Common Share**

Basic net loss per common share is computed using the weighted average number of shares of common stock and diluted net loss per common share is computed using the weighted average number of shares of common stock and common equivalent shares outstanding. Common equivalent shares related to stock options totaling 7,763,098 and 8,598,934 for the three months ended June 30, 2002 and 2001, respectively, and 8,943,000 and 8,599,000 for the six months ended June 30, 2002 and 2001, respectively, are excluded from the computation of diluted net loss per common share because their effect was antidilutive.

Basic and diluted net loss per common share for the three and six months ended June 30, 2001, include the effect of 744,740 shares issued to Computer Associates International, Inc. ( Computer Associates ) on June 24, 2002, as if the shares were issued and outstanding on June 8, 2001.

**3. Agreements with Computer Associates**

Pursuant to the purchase of all of the outstanding capital stock of Viewpoint Digital, Inc. ( Viewpoint Digital ) on September 8, 2000, the Company issued two contingent promissory notes to Computer Associates each in the

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**VIEWPOINT CORPORATION**
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)**

maximum amount of $15,000,000, but subject to reduction on the basis of the performance of the Viewpoint Digital assets. During 2001, the Company entered into certain agreements with Computer Associates whereby Computer Associates agreed to accept newly-issued shares of Viewpoint common stock having a value of $4,000,000, in partial repayment of the first contingent promissory note due June 8, 2001. In addition Computer Associates agreed to accept, at the Company s election, either cash or newly-issued shares of Viewpoint common stock at an issue price of $4.00 per share in repayment of any additional amounts due under the promissory note due June 8, 2001, and the first $8,943,000 of the $15,000,000 contingent promissory note due April 30, 2002.

In June 2002, Viewpoint issued 909,093 shares of Viewpoint common stock to Computer Associates in full satisfaction of the first contingent promissory note due June 8, 2001. The amount due Computer Associates under the promissory note due April 30, 2002 is approximately $2,928,000 and is reflected in due to related parties in the Company s consolidated balance sheet at June 30, 2002.

**4. Related Party Transactions**

During the three and six months ended June 30, 2002, the Company recorded revenues totaling $2,976,000 and $5,598,000, respectively, related to agreements, including reseller arrangements, with America Online, Inc. ( AOL ) and Computer Associates, both of whom have representatives on the Company s Board of Directors. The $5,598,000 of revenues for the six months ended June 30, 2002 includes approximately $3,500,000 due to a March 2002 amendment to a contract with AOL, which resulted in the Company recording revenues when payments are due, as contrasted to the partial deferral of those payments which would otherwise have occurred. As of June 30, 2002, the Company has $1,452,000 in accounts receivable and $507,000 in deferred revenue relating to transactions entered into with these related parties.

During the three and six months ended June 30, 2001, the Company recorded revenues totaling $198,000 and $356,000, respectively, related to agreements, including reseller arrangements, with Computer Associates.

**5. Goodwill and Intangible Assets**

Effective January 1, 2002, the Company completed the adoption of SFAS No. 141, Business Combinations, and SFAS No. 142, Goodwill and Other Intangible Assets. SFAS No. 141 requires all business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting. As required by SFAS No. 142, the Company discontinued amortizing the remaining balances of goodwill as of January 1, 2002. All remaining and future acquired goodwill will be subject to impairment tests annually, or earlier if indicators of potential impairment exist, using a fair-value-based approach. All other intangible assets will continue to be amortized over their estimated useful lives and assessed for impairment under SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. In conjunction with the implementation of SFAS No. 142, the Company complete