EVOLVING SYSTEMS INC
Form 10-Q
August 13, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x   **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended June 30, 2013

OR

o   **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: 0-24081

EVOLVING SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**84-1010843**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

9777 Pyramid Court, Suite 100 Englewood, Colorado	**80112**
(Address of principal executive offices)	(Zip Code)

(303) 802-1000

(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 o

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 o

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

Large accelerated filer o	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting companyx

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

As of August 7, 2013 there were 11,439,661 shares outstanding of Registrant s Common Stock (par value $0.001 per share).

EVOLVING SYSTEMS, INC.

Quarterly Report on Form 10-Q

June 30, 2013

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PART I   FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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EVOLVING SYSTEMS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands except share data)

(unaudited)

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	June 30, 2013	December 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$ 13,372	$ 8,844
Short-term restricted cash		53
Contract receivables, net of allowance for doubtful accounts of $70 at June 30, 2013 and December 31, 2012, respectively	5,601	4,803
Unbilled work-in-progress, net of allowance of $293 and $295 at June 30, 2013 and December 31, 2012, respectively	2,094	4,802
Prepaid and other current assets	1,002	1,133
Total current assets	22,069	19,635
Property and equipment, net	255	211
Amortizable intangible assets, net		204
Goodwill	15,538	16,510
Long-term deferred income taxes		27
Other long-term assets	2	6
Total assets	$ 37,864	$ 36,593
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Current portion of capital lease obligations	$ 4	$ 4
Accounts payable and accrued liabilities	2,857	3,833
Income taxes payable	400	308
Dividends payable	913	
Unearned revenue	3,350	1,596
Total current liabilities	7,524	5,741
Long-term liabilities:		
Capital lease obligations, net of current portion	14	16
Deferred income taxes	160	
Total liabilities	7,698	5,757
Commitments and contingencies		
Stockholders equity:		
Preferred stock, $0.001 par value; 2,000,000 shares authorized; no shares issued and outstanding as of June 30, 2013 and December 31, 2012		

Common stock, $0.001 par value; 40,000,000 shares authorized; 11,618,186 shares issued and 11,439,297 outstanding as of June 30, 2013 and 11,566,109 shares issued and 11,387,220 outstanding as of December 31, 2012		12	11
Additional paid-in capital		92,467	91,957
Treasury stock 178,889 shares as of June 30, 2013 and December 31, 2012, at cost		(1,253)	(1,253)
Accumulated other comprehensive loss		(4,733)	(3,297)
Accumulated deficit		(56,327)	(56,582)
Total stockholders equity		30,166	30,836
Total liabilities and stockholders equity	$	37,864 $	36,593

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

EVOLVING SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands except per share data)

(unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
REVENUE				
License fees and services	$ 3,518	$ 4,507	$ 8,025	$ 8,291
Customer support	2,267	2,147	4,429	4,271
Total revenue	5,785	6,654	12,454	12,562
COSTS OF REVENUE AND OPERATING EXPENSES				
Costs of license fees and services, excluding depreciation and amortization	1,301	1,524	2,837	3,342
Costs of customer support, excluding depreciation and amortization	401	387	709	747
Sales and marketing	1,245	1,223	2,546	2,564
General and administrative	768	994	1,663	1,907
Product development	684	778	1,397	1,507
Depreciation	37	79	74	152
Amortization	97	100	195	199
Total costs of revenue and operating expenses	4,533	5,085	9,421	10,418
Income from operations	1,252	1,569	3,033	2,144
Other income (expense)				
Interest income	3	29	6	50
Interest income, related party		100		532
Interest expense	(5)		(11)	(1)
Gain on sale of investments		891		891
Foreign currency exchange gain (loss)	188	46	145	(50)
Other income (expense), net	186	1,066	140	1,422
Income from operations before income taxes	1,438	2,635	3,173	3,566
Income tax expense	529	504	1,091	678
Net income	$ 909	$ 2,131	$ 2,082	$ 2,888
Basic income per common share	$ 0.08	$ 0.19	$ 0.18	$ 0.26
Diluted income per common share	$ 0.08	$ 0.19	$ 0.18	$ 0.25
Cash dividend declared per common share	$ 0.08	$ 1.70	$ 0.16	$ 1.75
Weighted average basic shares outstanding	11,423	11,261	11,416	11,213
Weighted average diluted shares outstanding	11,691	11,511	11,691	11,440

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

EVOLVING SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands except per share data)

(unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
Net income	$ 909	$ 2,131	$ 2,082	$ 2,888
Other comprehensive income (loss):				
Foreign currency translation gain (loss)	(288)	(683)	(1,436)	99
Unrealized gains (losses) on available-for-sale securities				
Unrealized holding gain (loss) arising during period		(319)		453
Other comprehensive income (loss), before tax	(288)	(1,002)	(1,436)	552
Income tax benefit (expense) related to components of other comprehensive income (loss)		120		(169)
Other comprehensive income (loss), net of tax	(288)	(882)	(1,436)	383
Comprehensive income	$ 621	$ 1,249	$ 646	$ 3,271

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

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EVOLVING SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

(in thousands, except share data)

(unaudited)

	Common Stock			Additional Paid-in Capital	Treasury Stock	Accumulated Other Comprehensive Loss	Accumulated (Deficit)	Total Stockholders Equity
	Shares		Amount					
Balance at December 31, 2012	**11,387,220**	**$**	**11**	**$ 91,957**	**$ (1,253)**	**$ (3,297)**	**$ (56,582)**	**$ 30,836**
Stock option exercises	38,330		1	112				113
Common Stock issued pursuant to the Employee Stock Purchase Plan	872			4				4
Stock-based compensation expense				154				154
Excess tax benefits from stock-based compensation				240				240
Restricted stock issuance, net of cancellations	12,875							
Common stock cash dividends							(1,827)	(1,827)
Net income							2,082	2,082
Foreign currency translation adjustment						(1,436)		(1,436)
Balance at June 30, 2013	**11,439,297**	**$**	**12**	**$ 92,467**	**$ (1,253)**	**$ (4,733)**	**$ (56,327)**	**$ 30,166**

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

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EVOLVING SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

		For the Six Months Ended June 30,		
		2013		2012
CASH FLOWS FROM OPERATING ACTIVITIES:				
Net income	$	2,082	$	2,888
Adjustments to reconcile net income to net cash provided by (used in) operating activities:				
Depreciation		74		152
Amortization of intangible assets		195		199
Amortization of debt issuance costs		10		
Stock based compensation		154		139
Accretion of discount on marketable securities				(6)
Gain on sale of marketable securities				(891)
Unrealized foreign currency transaction (gains) and losses, net		(145)		50
Provision for bad debt				187
Provision for deferred income taxes		173		71
Change in operating assets and liabilities:				
Contract receivables		(902)		(585)
Unbilled work-in-progress		2,569		(1,711)
Prepaid and other assets		68		466
Accounts payable and accrued liabilities		(729)		(190)
Unearned revenue		1,883		(1,009)
Net cash provided by (used in) operating activities		5,432		(240)
CASH FLOWS FROM INVESTING ACTIVITIES:				
Purchase of property and equipment		(133)		(57)
Proceeds from sale of marketable securities, related party				17,831
Restricted cash		53		
Net cash (used in) provided by investing activities		(80)		17,774
CASH FLOWS FROM FINANCING ACTIVITIES:				
Capital lease payments		(2)		(12)
Common stock cash dividends		(913)		(41,997)
Excess tax benefits from stock-based compensation		240		
Proceeds from the issuance of stock		116		353
Net cash used in financing activities		(559)		(41,656)
Effect of exchange rate changes on cash		(265)		(133)
Net increase (decrease) in cash and cash equivalents		4,528		(24,255)
Cash and cash equivalents at beginning of period		8,844		34,290
Cash and cash equivalents at end of period	$	13,372	$	10,035
Supplemental disclosure of non-cash financing transactions:				
Income taxes paid	$	106	$	693
Common stock dividend declared		913		19,725
Property and equipment purchased and included in accounts payable				5

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

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EVOLVING SYSTEMS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1   BASIS OF PRESENTATION

Organization   We are a provider of software solutions and services to the wireless, wireline and cable markets. We maintain long-standing relationships with many of the largest network operators worldwide. Our customers rely on us to develop, deploy, enhance, maintain and integrate complex, highly reliable software solutions for a range of Operations Support Systems (OSS). We offer software products and solutions focused on activation and provisioning: our service activation solution, *TertioTM* (TSA) used to activate complex bundles of voice, video and data services for traditional and next generation wireless and wireline networks; our SIM card activation solution, *Dynamic SIM Allocation TM* (DSA) used to dynamically allocate and assign resources to wireless devices that rely on SIM cards, and our connected devices activation solution, *Intelligent M2M Controller* (IMC) which supports the activation of M2M devices with intermittent or infrequent usage patterns.

Interim Consolidated Financial Statements   The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and in conformity with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X and the related rules and regulations of the Securities and Exchange Commission (SEC). Accordingly, certain information and note disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. However, we believe that the disclosures included in these financial statements are adequate to make the information presented not misleading. The unaudited condensed consolidated financial statements included in this document have been prepared on the same basis as the annual consolidated financial statements, and in our opinion reflect all adjustments, which include normal recurring adjustments necessary for a fair presentation in accordance with GAAP and SEC regulations for interim financial statements. The results for the three and six months ended June 30, 2013 are not necessarily indicative of the results that we will have for any subsequent period. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes to those statements for the year ended December 31, 2012 included in our Annual Report on Form 10-K.

Use of Estimates   The preparation of financial statements in conformity with GAAP requires us 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, as well as the reported amounts of revenue and expenses during the reporting period. We made estimates with respect to revenue recognition for estimated hours to complete projects accounted for using the percentage-of-completion method, allowance for doubtful accounts, income tax valuation allowance, fair values of long-lived assets, valuation of intangible assets and goodwill, useful lives for property, equipment and intangible assets, business combinations, capitalization of internal software development costs and fair value of stock-based compensation amounts. Actual results could differ from these estimates.

Foreign Currency   Our functional currency is the U.S. dollar. The functional currency of our foreign operations is the respective local currency for each foreign subsidiary. Assets and liabilities of foreign operations denominated in local currencies are translated at the spot rate in effect at the applicable reporting date. Our consolidated statements of operations are translated at the weighted average rate of exchange during the applicable period. The resulting unrealized cumulative translation adjustment is recorded as a component of accumulated other comprehensive income (loss) in stockholders equity. Realized and unrealized transaction gains and losses generated by transactions denominated in a currency different from the functional currency of the applicable entity are recorded in other income (loss) in the consolidated statements of operations in the period in which they occur.

Principles of Consolidation   The consolidated financial statements include the accounts of Evolving Systems, Inc. and subsidiaries, all of which are wholly owned. All significant intercompany transactions and balances have been eliminated in consolidation.

Goodwill   Goodwill is the excess of acquisition cost of an acquired entity over the fair value of the identifiable net assets acquired. Goodwill is not amortized, but tested for impairment annually or whenever indicators of impairment exist. These indicators may include a significant change in the business climate, legal factors, operating performance indicators, competition, sale or disposition of a significant portion of the business or other factors. Application of the goodwill impairment test requires judgment, including the identification of reporting units, assignment of assets and liabilities to reporting units, assignment of goodwill to reporting units, and determination of the fair value of each reporting unit.

We performed our annual goodwill impairment test as of July 31, 2012 and determined that no impairment of our goodwill had occurred. As of the date this report was issued, we are in progress of completing our annual goodwill impairment test as of July 31, 2013.

Intangible Assets   Amortizable intangible assets consist primarily of purchased software and licenses, customer contracts and relationships, trademarks and tradenames, and business partnerships acquired in conjunction with our purchase of Tertio Telecoms Ltd. (Evolving Systems U.K.). These assets are amortized using the straight-line method over their estimated lives.

We assess the impairment of identifiable intangibles if events or changes in circumstances indicate that the carrying value of the asset may not be recoverable. If we determine that the carrying value of intangibles and/or long-lived assets may not be recoverable, we compare the estimated undiscounted cash flows expected to result from the use of the asset and its eventual disposition to the asset s carrying amount. If an amortizable intangible or long-lived asset is not deemed to be recoverable, we recognize an impairment loss representing the excess of the asset s carrying value over its estimated fair value.

Fair Value Measurements   Fair value is the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is estimated by applying the following hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and signifi