

VONAGE HOLDINGS CORP

Form 10-Q/A

March 17, 2008

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**Form 10-Q/A**

**Amendment No. 1**

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

**For the Quarterly Period Ended September 30, 2007**

**or**

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

**For the Transition Period From \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number 001-32887**

**VONAGE HOLDINGS CORP.**

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(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of incorporation or organization)

**11-3547680**  
(IRS Employer Identification No.)

**23 Main Street, Holmdel, NJ**  
(Address of principal executive offices)

**07733**  
(Zip Code)

**Registrant's telephone number, including area code: (732) 528-2600**

**(Former name, former address and former fiscal year, if changed since last report): Not Applicable**

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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

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

**Class**  
Common Stock, par value \$0.001

**Outstanding at October 31, 2007**  
155,863,949 shares

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**EXPLANATORY NOTE**

This Amendment No. 1 to our Quarterly Report on Form 10-Q for the three and nine months ended September 30, 2007 is being filed to reflect a correction of the amount of share-based compensation expense recorded by us for the three and nine months ended September 30, 2007. The consolidated financial statements and Note 1 in Item 1 of Part I and Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 2 of Part I are amended and restated to reflect the correct amount of share-based compensation for the three and nine months ended September 30, 2007. For further discussion regarding the restatement, see Note 1 to our consolidated financial statements. In light of the restatement of our financial results, our interim chief executive officer and chief financial officer re-evaluated our disclosure controls and procedures as of September 30, 2007 and concluded that our disclosure controls and procedures were not effective as of such date due to a material weakness in internal control over financial reporting. Please see Item 4 of Part I for a discussion of our management's re-evaluation and conclusions.

This Amendment No. 1 did not result in a change in our previously reported revenues, cash flow from operations or total cash and cash equivalents shown in our consolidated financial statements in this Amendment No. 1. This Amendment No. 1 continues to speak as of the date of the original Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2007, and we have not updated or amended disclosure contained herein to reflect events that have occurred since filing the original Form 10-Q, or modified or updated those disclosures in any way other than as described in the preceding paragraph. Accordingly, this Amendment No. 1 should be read in conjunction with our filings made with the Securities and Exchange Commission subsequent to the filing of the original Form 10-Q on November 14, 2007.

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**Table of Contents****Part I Financial Information****Item 1. Financial Statements****VONAGE HOLDINGS CORP.****CONSOLIDATED BALANCE SHEETS****(In thousands, except par value)****(Unaudited)**

	<b>September 30, 2007 (as restated)</b>	<b>December 31, 2006</b>
<b>Assets</b>		
<b>Assets</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 129,010	\$ 210,253
Marketable securities	148,734	289,483
Accounts receivable, net of allowance of \$1,400 and \$476, respectively	21,823	16,544
Inventory, net of allowance of \$2,131 and \$1,270, respectively	19,898	24,390
Deferred customer acquisition costs, current	17,060	13,022
Prepaid expenses and other current assets	23,564	16,080
Restricted cash	78,146	
<b>Total current assets</b>	<b>438,235</b>	<b>569,772</b>
Property and equipment, net of accumulated depreciation	127,856	128,247
Deferred customer acquisition costs, non-current	38,635	34,067
Deferred financing costs, net	6,371	7,861
Restricted cash	31,134	8,042
Due from related parties	4	60
Intangible assets, net	8,346	4,300
Other assets	15,181	5,175
<b>Total assets</b>	<b>\$ 665,762</b>	<b>\$ 757,524</b>
<b>Liabilities and Stockholders Equity (Deficit)</b>		
<b>Liabilities</b>		
<b>Current liabilities:</b>		
Accounts payable	\$ 58,121	\$ 58,899
Accrued expenses	273,698	161,505
Deferred revenue, current portion	51,038	38,504
Current maturities of capital lease obligations	1,018	1,020
<b>Total current liabilities</b>	<b>383,875</b>	<b>259,928</b>
Convertible notes, net	253,310	253,430
Deferred revenue, net of current portion	43,023	37,730
Capital lease obligations, net of current maturities	22,483	23,235
Other liability, net of current portion	26,000	
<b>Total liabilities</b>	<b>728,691</b>	<b>574,323</b>

**Commitments and Contingencies**

**Stockholders' Equity (Deficit)**

Common stock, par value \$0.001 per share; authorized 596,950 shares at September 30, 2007 and December 31, 2006;

157,235 and 156,353 shares issued at September 30, 2007 and December 31, 2006, respectively;

155,882 and 155,059 shares outstanding at September 30, 2007 and December 31, 2006, respectively

	157	156
Additional paid-in capital	928,907	922,097
Stock subscription receivable	(5,273)	(5,721)
Accumulated deficit	(974,445)	(720,857)
Treasury stock, at cost, 1,353 shares at September 30, 2007 and 1,294 shares at December 31, 2006	(12,428)	(12,342)
Accumulated other comprehensive income (loss)	153	(132)

<b>Total stockholders' equity (deficit)</b>	<b>(62,929)</b>	<b>183,201</b>
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Total liabilities and stockholders' equity (deficit)	\$ 665,762	\$ 757,524
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The accompanying notes are an integral part of the consolidated financial statements.

**Table of Contents****VONAGE HOLDINGS CORP.****CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except per share amounts)****(Unaudited)**

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
	<b>(as restated)</b>		<b>(as restated)</b>	
<b>Operating Revenues:</b>				
Telephony services	\$ 203,724	\$ 155,611	\$ 593,561	\$ 405,732
Customer equipment and shipping	6,810	6,235	18,815	20,202
	210,534	161,846	612,376	425,934
<b>Operating Expenses:</b>				
Direct cost of telephony services (excluding depreciation and amortization of \$4,312, \$3,022, \$12,616 and \$8,707, respectively)	54,463	41,396	162,364	119,753
Royalty	11,139		32,606	
Total direct cost of telephony services	65,602	41,396	194,970	119,753
Direct cost of goods sold	17,057	16,934	41,633	50,561
Selling, general and administrative	214,139	72,052	382,933	191,036
Marketing	61,885	91,316	220,641	269,768
Depreciation and amortization	8,563	5,946	24,613	16,645
	367,246	227,644	864,790	647,763
Loss from operations	(156,712)	(65,798)	(252,414)	(221,829)
<b>Other Income (Expense):</b>				
Interest income	4,238	7,721	15,066	14,442
Interest expense	(5,424)	(3,999)	(15,700)	(13,977)
Other, net	(36)	(108)	(69)	(116)
	(1,222)	3,614	(703)	349
Loss before income tax benefit (expense)	(157,934)	(62,184)	(253,117)	(221,480)
Income tax benefit (expense)	(94)		(471)	
Net loss	\$ (158,028)	\$ (62,184)	\$ (253,588)	\$ (221,480)
<b>Net loss per common share:</b>				
Basic and diluted	\$ (1.01)	\$ (0.40)	\$ (1.63)	\$ (2.99)
<b>Weighted-average common shares outstanding:</b>				
Basic and diluted	155,784	154,775	155,482	73,955

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



**Table of Contents****VONAGE HOLDINGS CORP.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)****(Unaudited)**

	<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>
	<b>(as restated)</b>	
<b>Cash flows from operating activities:</b>		
Net loss	\$ (253,588)	\$ (221,480)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	23,159	16,412
Amortization of intangibles	1,454	233
Beneficial conversion on interest in kind on convertible notes	32	22
Accrued interest	597	3,295
Allowance for doubtful accounts	1,087	191
Allowance for obsolete inventory	1,443	827
Amortization of deferred financing costs	1,490	1,503
Loss on disposal of fixed assets	118	16
Share-based compensation	5,879	19,980
Other		(49)
Changes in operating assets and liabilities:		
Accounts receivable	(6,220)	(6,608)
Inventory	3,350	(2,764)
Prepaid expenses and other current assets	(8,047)	(13,512)
Deferred customer acquisition costs	(8,284)	(16,908)
Due from related parties	74	25
Other assets	185	(129)
Accounts payable	(1,108)	40,732
Accrued expenses	106,147	(10,159)
Deferred revenue	17,243	27,681
Other liability	26,000	
<b>Net cash provided by (used in) operating activities</b>	<b>(88,989)</b>	<b>(160,692)</b>
<b>Cash flows from investing activities:</b>		
Capital expenditures	(19,981)	(32,472)
Purchase of intangible assets		(5,268)
Purchase of marketable securities	(210,325)	(559,507)
Maturities and sales of marketable securities	351,032	303,043
Acquisition and development of software assets	(12,737)	(1,126)
Increase in restricted cash	(101,160)	(1,870)
<b>Net cash provided by (used in) investing activities</b>	<b>6,829</b>	<b>(297,200)</b>
<b>Cash flows from financing activities:</b>		
Principal payments on capital lease obligations	(754)	(593)
Proceeds from notes issuance		2,047
Debt issuance costs		(283)

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Proceeds from subscription receivable, net	279	131
Proceeds from common stock issuance, net		493,497
Purchase of treasury stock		(11,723)
Payments for directed share program, net	169	(4,017)
Proceeds from exercise of stock options	780	290
<b>Net cash provided by (used in) financing activities</b>	<b>474</b>	<b>479,349</b>
Effect of exchange rate changes on cash	443	10
<b>Net change in cash and cash equivalents</b>	<b>(81,243)</b>	<b>21,467</b>
Cash and cash equivalents, beginning of period	210,253	132,549
<b>Cash and cash equivalents, end of period</b>	<b>\$ 129,010</b>	<b>\$ 154,016</b>

**Supplemental disclosures of cash flow information:**

Cash paid during the periods for:

Interest	\$ 15,167	\$ 8,501
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The accompanying notes are an integral part of the consolidated financial statements.

**Table of Contents****VONAGE HOLDINGS CORP.****CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY (DEFICIT)**

(In thousands)

(Unaudited)

(as restated)

	Common Stock	Additional Paid-in Capital	Stock Subscription Receivable	Accumulated Deficit	Treasury Stock	Accumulated Other Comprehensive Loss	Total
Balance at December 31, 2006	\$ 156	\$ 922,097	\$ (5,721)	\$ (720,857)	\$ (12,342)	\$ (132)	\$ 183,201
Stock option exercises	1	779					780
Share-based compensation		5,879					5,879
Share-based award activity					(86)		(86)
Convertible notes converted into common stock		152					152
Directed share program transactions, net			169				169
Stock subscription receivable payments			279				279
Comprehensive loss:							
Change in unrealized gain (loss) on available-for-sale investments						(42)	(42)
Foreign currency translation adjustment						327	327
Net loss				(253,588)			(253,588)
Total comprehensive loss				(253,588)		285	(253,303)
Balance at September 30, 2007	\$ 157	\$ 928,907	\$ (5,273)	\$ (974,445)	\$ (12,428)	\$ 153	\$ (62,929)

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

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**VONAGE HOLDINGS CORP.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(In thousands, except per share amounts)**

**(Unaudited)**

**Note 1. Restatement of Condensed Consolidated Financial Statements**

*Background Information*

In December 2004, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 123(R) ( SFAS No. 123(R) ) *Share-Based Payment*. SFAS No. 123(R) requires all share-based payments to employees, including stock awards, to be recognized as expenses in the issuer's financial statements based on the fair values of those payments, reduced as appropriate based on any estimated forfeitures. Share-based compensation expense recognized during a period is based on the value of the portion of share-based payment awards that is ultimately expected to vest during the period. However, SFAS No. 123(R) requires that compensation cost recognized at any date must be at least equal to the amount attributable to awards that are vested at that date.

Due to the departure of our former chief executive officer, certain senior executives and other personnel primarily as a result of the reduction in force during the second and third quarters of 2007, there was a corresponding forfeiture of a large number of stock awards, and we determined that actual forfeitures as a result of these actions exceeded previous estimates. As a result, non-cash stock compensation expense should have been reduced concurrent with the resignation of these employees and a reduction of stock-based compensation as required by SFAS No. 123(R) should have been recorded at that time.

In February 2008, our management, after consultation with our audit committee of the board of directors and our independent public accounting firm, determined that it was necessary to restate our previously issued consolidated financial statements for the three and nine months ended September 30, 2007 in order to correct the amount of share-based compensation expense recorded by us for those periods.

*Restatement*

The restatement has been accounted for in accordance with SFAS No. 154, *Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3*, as a revision of previously issued financial statements to reflect the correction of an error.

We have calculated the amount of the necessary adjustments resulting from the restatement to be approximately \$3,800 and \$14,200 for the three and nine months ended September 30, 2007, respectively, which amounts should have been recorded as decreases in non-cash share-based compensation expense within our operating expenses. Previously, in the Form 10-Q, we reported non-cash share-based compensation expense of \$6,228 and \$20,079 for the three and nine months ended September 30, 2007, respectively. As a result, after applying the necessary cumulative adjustment referenced above, our non-cash share-based compensation expense for the three and nine months ended September 30, 2007 are \$2,428 and \$5,879, respectively.

This restatement did not result in a change in our previously reported revenues, cash flow from operations or total cash and cash equivalents shown in the consolidated financial statements for or as of the three and nine months ended September 30, 2007. Instead, the resulting decrease in non-cash share-based compensation expense results in a decrease of \$3,800 and \$14,200 in our net loss for the three and nine months ended September 30, 2007, respectively. In addition, because the amount of decrease in non-cash share-based compensation expense had an effect of decreasing both our accumulated deficit and additional paid in capital, there was no net effect on our consolidated stockholders' equity (deficit) at September 30, 2007.

There is no difference between the gross adjustment to non-cash share-based compensation described herein and the net effect after taxes as we have a history of net losses and a valuation allowance has been recorded to offset the net deferred tax assets at September 30, 2007.

**Table of Contents****Consolidated Balance Sheet Adjustments**

The following is a summary of the adjustments to our previously issued unaudited consolidated balance sheet at September 30, 2007.

	September 30, 2007		
	as previously reported	adjustments	as restated
<b>Assets</b>			
<b>Assets</b>			
Current assets:			
Cash and cash equivalents	\$ 129,010		\$ 129,010
Marketable securities	148,734		148,734
Accounts receivable, net of allowance	21,823		21,823
Inventory, net of allowance	19,898		19,898
Deferred customer acquisition costs, current	17,060		17,060
Prepaid expenses and other current assets	23,564		23,564
Restricted cash	78,146		78,146
<b>Total current assets</b>	<b>438,235</b>		<b>438,235</b>
Property and equipment, net of accumulated depreciation	127,856		127,856
Deferred customer acquisition costs, non-current	38,635		38,635
Deferred financing costs, net	6,371		6,371
Restricted cash	31,134		31,134
Due from related parties	4		4
Intangible assets, net	8,346		8,346
Other assets	15,181		15,181
<b>Total assets</b>	<b>\$ 665,762</b>		<b>\$ 665,762</b>
<b>Liabilities and Stockholders Equity (Deficit)</b>			
<b>Liabilities</b>			
Current liabilities:			
Accounts payable	\$ 58,121		\$ 58,121
Accrued expenses	273,698		273,698
Deferred revenue, current portion	51,038		51,038
Current maturities of capital lease obligations	1,018		1,018
Convertible notes, net			
<b>Total current liabilities</b>	<b>383,875</b>		<b>383,875</b>
Convertible notes, net	253,310		253,310
Deferred revenue, net of current portion	43,023		43,023
Capital lease obligations, net of current maturities	22,483		22,483
Other liability, net of current portion	26,000		26,000
<b>Total liabilities</b>	<b>728,691</b>		<b>728,691</b>
<b>Commitments and Contingencies</b>			
<b>Stockholders Equity (Deficit)</b>			
Common stock	157		157
Additional paid-in capital	943,107	(14,200)	928,907
Stock subscription receivable	(5,273)		(5,273)
Accumulated deficit	(988,645)	14,200	(974,445)
Treasury stock	(12,428)		(12,428)
Accumulated other comprehensive income (loss)	153		153

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Total stockholders' equity (deficit)	(62,929)	(62,929)
Total liabilities and stockholders' equity (deficit)	\$ 665,762	\$ 665,762

**Table of Contents****Consolidated Statements of Operations Adjustments**

The following is a summary of the adjustments to our previously issued unaudited consolidated statements of operations for the three and nine months ended September 30, 2007.

	Three Months Ended September 30, 2007			Nine Months Ended September 30, 2007 as		
	as previously reported	adjustments	as restated	previously reported	adjustments	as restated
<b>Operating Revenues:</b>						
Telephony services	\$ 203,724		\$ 203,724	\$ 593,561		\$ 593,561
Customer equipment and shipping	6,810		6,810	18,815		18,815
	210,534		210,534	612,376		612,376
<b>Operating Expenses:</b>						
Direct cost of telephony services	54,463		54,463	162,364		162,364
Royalty	11,139		11,139	32,606		32,606
Total cost of telephony services	65,602		65,602	194,970		194,970
Direct cost of goods sold	17,057		17,057	41,633		41,633
Selling, general and administrative	217,939	(3,800)	214,139	397,133	(14,200)	382,933
Marketing	61,885		61,885	220,641		220,641
Depreciation and amortization	8,563		8,563	24,613		24,613
	371,046		367,246	878,990		864,790