LogMeIn, Inc.
Form 10-Q
October 28, 2010

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2010

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: 001-34391

LOGMEIN, INC.

(Exact name of registrant as specified in its charter)

Delaware	**20-1515952**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
500 Unicorn Park Drive Woburn, Massachusetts	**01801**
(Address of principal executive offices)	(Zip Code)

781-638-9050

(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 þ 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 o No o

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

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

As of October 20, 2010, there were 23,681,570 shares of the registrant s Common Stock, par value $.01 per share, outstanding.

LOGMEIN, INC.
INDEX

	PAGE NUMBER
PART I. FINANCIAL INFORMATION	
ITEM 1: Financial Statements	2
Condensed Consolidated Balance Sheets	2
Condensed Consolidated Statements of Income	3
Condensed Consolidated Statements of Cash Flows	4
Notes to Condensed Consolidated Financial Statements	5
ITEM 2: Management s Discussion and Analysis of Financial Condition and Results of Operations	13
ITEM 3: Quantitative and Qualitative Disclosures about Market Risk	20
ITEM 4: Controls and Procedures	20
PART II. OTHER INFORMATION	
ITEM 1: Legal Proceedings	21
ITEM 1A: Risk Factors	21
ITEM 2: Unregistered Sales of Equity Securities and Use of Proceeds	31
ITEM 6: Exhibits	32
Signatures	33
EX-31.1	
EX-31.2	
EX-32.1	
EX-32.2	

Table of Contents

Part I. Financial Information
Item 1. Financial Statements

LogMeIn, Inc.
Condensed Consolidated Balance Sheets

	December 31, 2009	September 30, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	$ 100,290,001	$ 75,640,381
Marketable securities	29,956,204	80,374,944
Accounts receivable (net of allowance for doubtful accounts of $83,000 and $108,000 as of December 31, 2009 and September 30, 2010, respectively)	4,149,645	5,826,595
Prepaid expenses and other current assets (including $101,000 and $61,000 of non-trade receivable due from related party at December 31, 2009 and September 30, 2010, respectively)	1,834,244	2,159,748
Deferred income tax assets		2,056,138
Total current assets	136,230,094	166,057,806
Property and equipment, net	4,859,139	5,553,783
Restricted cash	373,184	357,361
Intangibles, net	750,915	645,244
Goodwill	615,299	615,299
Other assets	29,918	24,277
Deferred income tax assets		4,602,568
Total assets	$ 142,858,549	$ 177,856,338
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 2,328,223	$ 3,549,515
Accrued liabilities	7,323,176	8,883,719
Deferred revenue, current portion	32,190,539	39,478,928
Total current liabilities	41,841,938	51,912,162
Deferred revenue, net of current portion	1,912,329	982,651
Other long-term liabilities	594,931	470,683
Total liabilities	44,349,198	53,365,496
Commitments and contingencies (Note 9)		
Stockholders equity:		
Common stock, $0.01 par value 75,000,000 shares authorized as of December 31, 2009 and September 30, 2010; 22,448,808 and 23,624,045 shares outstanding as of December 31, 2009 and September 30, 2010, respectively	224,488	236,240
Additional paid-in capital	122,465,372	132,669,428
Accumulated deficit	(24,182,960)	(8,471,204)

Accumulated other comprehensive income	2,451	56,378
Total stockholders equity	98,509,351	124,490,842
Total liabilities and stockholders equity	$ 142,858,549	$ 177,856,338

See notes to condensed consolidated financial statements.

Table of Contents

LogMeIn, Inc.
Condensed Consolidated Statements of Income

	Three Months September 30,		Nine Months Ended September 30,	
	2009	2010	2009	2010
Revenue (including $1,485,000, $4,521,000, $1,738,000 and $4,711,000 from a related party during the three and nine months ended September 30, 2009 and 2010, respectively)	$ 18,970,752	$ 25,349,529	$ 54,174,989	$ 70,166,783
Cost of revenue	1,909,976	2,243,288	5,507,722	6,728,223
Gross profit	17,060,776	23,106,241	48,667,267	63,438,560
Operating expenses				
Research and development	3,578,728	3,560,484	9,487,212	10,874,451
Sales and marketing	9,059,326	11,506,645	26,378,524	32,153,542
General and administrative	2,344,130	2,909,644	5,786,568	8,390,143
Amortization of intangibles	81,929	81,929	245,787	245,787
Total operating expenses	15,064,113	18,058,702	41,898,091	51,663,923
Income from operations	1,996,663	5,047,539	6,769,176	11,774,637
Interest income, net	42,017	202,369	66,871	456,319
Other expense	(140,979)	(66,902)	(300,897)	(102,337)
Income before income taxes	1,897,701	5,183,006	6,535,150	12,128,619
Benefit (provision) for income taxes	(47,846)	(1,188,475)	(212,021)	3,583,137
Net income	1,849,855	3,994,531	6,323,129	15,711,756
Accretion of redeemable convertible preferred stock	(49,084)		(1,311,225)	
Net income attributable to common stockholders	$ 1,800,771	$ 3,994,531	$ 5,011,904	$ 15,711,756
Net income attributable to common stockholders per share:				
Basic	$ 0.08	$ 0.17	$ 0.28	$ 0.68
Diluted	$ 0.07	$ 0.16	$ 0.27	$ 0.64
Weighted average shares outstanding:				
Basic	21,372,510	23,435,172	9,857,792	23,072,983
Diluted	23,472,881	24,882,767	11,675,094	24,734,943

See notes to condensed consolidated financial statements.

Table of Contents

LogMeIn, Inc.
Condensed Consolidated Statements of Cash Flows

	Nine Months Ended September 30,	
	2009	2010
Cash flows from operating activities		
Net income	$ 6,323,129	$ 15,711,756
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	2,278,525	2,737,594
Amortization of premiums on investments		159,756
Provision for bad debts	85,000	65,000
Deferred income taxes	12,390	(3,755,556)
Income tax benefit from the exercise of stock options		(2,898,577)
Stock-based compensation	2,115,522	3,536,185
Loss (gain) on disposal of equipment	1,006	(1,882)
Changes in assets and liabilities:		
Accounts receivable	185,247	(1,741,950)
Prepaid expenses and other current assets	(458,694)	(325,505)
Other assets	(9,676)	5,641
Accounts payable	478,625	849,586
Accrued liabilities	1,474,079	1,613,851
Deferred revenue	3,605,340	6,358,711
Other long-term liabilities	347,978	(124,248)
Net cash provided by operating activities	16,438,471	22,190,362
Cash flows from investing activities		
Purchases of marketable securities		(155,388,550)
Proceeds from maturity of marketable securities		105,000,000
Purchases of property and equipment	(2,927,539)	(2,434,040)
Intangible asset additions		(376,638)
(Increase) decrease in restricted cash and deposits	(2,724)	5,118
Net cash used in investing activities	(2,930,263)	(53,194,110)
Cash flows from financing activities		
Proceeds from issuance of common stock in connection with initial public offering, net of issuance costs of $1,273,000	84,286,993	
Payments of issuance costs related to secondary offering of common stock		(195,840)
Proceeds from issuance of common stock upon option exercises	166,088	3,776,705
Income tax benefit from the exercise of stock options		2,898,577
Net cash provided by financing activities	84,453,081	6,479,442
Effect of exchange rate changes on cash and cash equivalents and restricted cash	132,878	(125,314)

Net increase (decrease) in cash and cash equivalents	98,094,167	(24,649,620)
Cash and cash equivalents, beginning of period	22,912,981	100,290,001
Cash and cash equivalents, end of period	$ 121,007,148	$ 75,640,381
Supplemental disclosure of cash flow information		
Noncash investing and financing activities		
Purchases of property and equipment included in accounts payable and accrued liabilities	$ 80,265	$ 677,646
Accretion of redeemable convertible preferred stock	$ 1,311,226	
Deferred stock offering costs included in accounts payable and accrued liabilities	$ 110,751	
Conversion of redeemable preferred stock to common stock	$ 36,154,494	

See notes to condensed consolidated financial statements.

4

Table of Contents

LogMeIn, Inc.
Notes to Condensed Consolidated Financial Statements

1. Nature of the Business

LogMeIn, Inc. (the Company) develops and markets a suite of remote access, remote support, and collaboration solutions that provide instant, secure connections between Internet enabled devices. The Company s product line includes Gravity , LogMeIn Free®, LogMeIn Pro[2]®, LogMeIn® Central , LogMeIn Rescue®, LogMeIn® Rescue+Mobile , LogMeIn Backup®, LogMeIn® Ignition[SM], LogMeIn Hamachi®, join.me and RemotelyAnywhere®. The Company is based in Woburn, Massachusetts with wholly-owned subsidiaries in Hungary, The Netherlands, Australia, England and Brazil.

2. Summary of Significant Accounting Policies

Principles of Consolidation The accompanying condensed consolidated financial statements include the results of operations of the Company and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation. The Company has prepared the accompanying consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP).

Unaudited Interim Condensed Consolidated Financial Statements The accompanying condensed consolidated financial statements and the related interim information contained within the notes to the condensed consolidated financial statements are unaudited and have been prepared in accordance with GAAP and applicable rules and regulations of the Securities and Exchange Commission for interim financial information. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. The accompanying unaudited condensed consolidated financial statements should be read along with the Company s audited financial statements included in the Company s Annual Report on Form 10-K, filed with the Securities and Exchange Commission on February 26, 2010. The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and in the opinion of management, reflect all adjustments, consisting of normal and recurring adjustments, necessary for the fair presentation of the Company s financial position, results of operations and cash flows for the interim periods presented. The results for the interim periods presented are not necessarily indicative of future results. The Company considers events or transactions that occur after the balance sheet date but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure.

Use of Estimates The preparation of condensed consolidated financial statements in conformity with GAAP requires management 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 and the reported amounts of revenue and expenses during the reporting period. By their nature, estimates are subject to an inherent degree of uncertainty. Actual results could differ from those estimates.

Marketable Securities The Company s marketable securities are classified as available-for-sale and are carried at fair value with the unrealized gains and losses reported as a component of accumulated other comprehensive income in stockholders equity. Realized gains and losses and declines in value judged to be other than temporary are included as a component of earnings based on the specific identification method. Fair value is determined based on quoted market prices. At December 31, 2009 and September 30, 2010, marketable securities consisted of U.S. government agency securities that have remaining maturities within two years and have an aggregate amortized cost of $30,009,895 and $80,238,690 and an aggregate fair value of $29,956,204 and $80,374,944, including $0 and $141,934 of unrealized gains and $53,691 and $5,680 of unrealized losses, respectively.

Revenue Recognition The Company derives revenue primarily from subscription fees related to its LogMeIn premium services and from the licensing of its Ignition for iPhone, iPad and Android software products and RemotelyAnywhere software and related maintenance.

Revenue from the Company s LogMeIn premium services is recognized on a daily basis over the subscription term as the services are delivered, provided that there is persuasive evidence of an arrangement, the fee is fixed or determinable and collectability is deemed reasonably assured. Subscription periods range from monthly to four years, but are generally one year in duration. The Company s software cannot be run on another entity s hardware nor do customers have the right to take possession of the software and use it on their own or another entity s hardware.

The Company recognizes revenue from the bundled delivery of its RemotelyAnywhere software product and related maintenance ratably, on a daily basis, over the term of the maintenance contract, generally one year, when there is persuasive evidence of an arrangement, the product has been provided to the customer, the collection of the fee is probable, and the amount of fees to be paid by the customer is fixed or determinable. The Company currently does not have vendor-specific objective evidence for the fair value of its maintenance arrangements and therefore the license and maintenance are bundled together. The Company recognizes revenue from the sale of its Ignition for iPhone, iPad and Android software product which is sold as a perpetual license and is recognized when there is persuasive evidence of an arrangement, the product has been provided to the customer, the collection of the fee is probable, and the amount of fees to be paid by the customer is fixed or determinable.

The Company s multi-element arrangements typically include multiple deliverables by the Company such as subscription and professional services, including development services. Agreements with multiple element deliverables are analyzed to determine if fair value exists for each element on a stand-alone basis. If the fair value of each deliverable is determinable then revenue is recognized separately when or as the services are delivered, or if applicable, when milestones associated with the deliverable are achieved and accepted by the customer. If the fair value of any of the undelivered performance obligations cannot be determined, the arrangement is accounted for as a single element and the

Table of Contents

Company recognizes revenue on a straightline basis over the period in which the Company expects to complete its performance obligations under the agreement.

Concentrations of Credit Risk and Significant Customers The Company s principal credit risk relates to its cash, cash equivalents, marketable securities, restricted cash, and accounts receivable. Cash, cash equivalents, and restricted cash are deposited primarily with financial institutions that management believes to be of high-credit quality and custody of its marketable securities is with an accredited financial institution. To manage accounts receivable credit risk, the Company regularly evaluates the creditworthiness of its customers and maintains allowances for potential credit losses. To date, losses resulting from uncollected receivables have not exceeded management s expectations.

As of September 30, 2010, one customer accounted for 13% of accounts receivable, and no customers accounted for more than 10% of revenue for the three or nine months ended September 30, 2009 and 2010. At December 30, 2009, there were no customers that accounted for 10% or more of accounts receivable.

Foreign Currency Translation The functional currency of operations outside the United States of America is deemed to be the currency of the local country. Accordingly, the assets and liabilities of the Company s foreign subsidiaries are translated into United States dollars using the period-end exchange rate, and income and expense items are translated using the average exchange rate during the period. Cumulative translation adjustments are reflected as a separate component of stockholders equity. Foreign currency transaction gains and losses are charged to operations. The Company had foreign currency losses of approximately $141,000 and $67,000 for the three months ended September 30, 2009 and 2010, respectively and approximately $301,000 and $102,000 for the nine months ended September 30, 2009 and 2010, respectively.

Stock-Based Compensation Stock-based compensation is measured based upon the grant date fair value of the award and recognized as an expense in the financial statements over the vesting period of the award. The Company uses the Black-Scholes option pricing model to estimate the grant date fair value of stock based awards.

Income Taxes Deferred income taxes are provided for the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, and operating loss carry-forwards and credits using enacted tax rates expected to be in effect in the years in which the differences are expected to reverse. At each balance sheet date, the Company assesses the likelihood that deferred tax assets will be realized, and recognizes a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction. As of December 31, 2009 and March 31, 2010, the Company provided a full valuation allowance against its deferred tax assets as it believed the objective and verifiable evidence of its historical pretax net losses outweighed the positive evidence of its pre-tax income for the year ended December 31, 2009 and the three months ended March 31, 2010 and forecasted future results.

At June 30, 2010, the Company reassessed the need for a valuation allowance against its deferred tax assets and concluded that it was more likely than not that it would be able to realize certain of its deferred tax assets primarily as a result of continued profitability and forecasted future results. Accordingly, the Company reversed its valuation allowance related to its U.S. and certain foreign deferred tax assets and recorded an income tax benefit of approximately $5,572,000 for the three months ended June 30, 2010. As of September 30, 2010, the Company maintained a full valuation allowance against the deferred tax assets of its Hungarian subsidiary.

The Company evaluates its uncertain tax positions based on a determination of whether and how much of a tax benefit taken by the Company in its tax filings or positions is more likely than not to be realized. Potential interest and penalties associated with any uncertain tax positions are recorded as a component of income tax expense. Through September 30, 2010, the Company has not identified any material uncertain tax positions for which liabilities would be required.

Comprehensive Income Comprehensive income is the change in stockholders equity during a period relating to transactions and other events and circumstances from non-owner sources and currently consists of net income, foreign currency translation adjustments and unrealized gains and losses on available-for-sale securities.

Comprehensive income was calculated as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2010	2009	2010
Net income	$ 1,849,855	$ 3,994,531	$ 6,323,129	$ 15,711,756
Cumulative translation adjustments	98,557	611,064	140,588	(136,019)
Unrealized gain on available-for-sale securities		46,894		189,946
Comprehensive income	$ 1,948,412	$ 4,652,489	$ 6,463,717	$ 15,765,683

Net Income Attributable to Common Stockholders Per Share The Company used the two-class method to compute net income per share for the three and nine month periods ended September 30, 2009, because the Company had previously issued securities, other than common stock, that contractually entitled the holders to participate in dividends and earnings of the company. The two class method requires earnings available to common stockholders for the period, after an allocation of earnings to participating securities, to be allocated between common and participating securities based upon their respective rights to receive distributed and undistributed earnings. The Company s convertible preferred stock was a participating security as it shared in any dividends paid to common stockholders. Such participating securities were automatically converted to common stock upon the Company s IPO in July 2009. Basic net income attributable to common stockholders per

Table of Contents

share was computed after allocation of earnings to the convertible preferred stock (losses are not allocated) by using the weighted average number common shares outstanding for the period.

The following potential common shares were excluded from the computation of diluted net income per share attributable to common stockholders because they had an anti-dilutive impact:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2010	2009	2010
Options to purchase common stock	1,034,373	324,150	1,034,373	1,029,350
Conversion of redeemable convertible preferred stock (1)	12,360,523		12,360,523	
Total options and conversion of convertible preferred stock	13,394,896	324,150	13,394,896	1,029,350

(1) The redeemable convertible preferred stock was considered anti-dilutive for the period prior to the Company s IPO in July 2009. Subsequent to the conversion, it is included in common stock.

Basic and diluted net income per share was calculated as follows:

	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2009
Basic net income per share		
Numerator		
Net income	1,849,855	6,323,129
Accretion of redeemable convertible preferred stock	(49,084)	(1,311,225)
Net income allocated to redeemable convertible preferred stock	(51,167)	(2,466,543)
Net income, as adjusted	$ 1,749,604	$ 2,545,361
Denominator		
Weighted average common shares outstanding, basic	21,372,510	9,202,277
Basic net income per share	$ 0.08	$ 0.28

		Three Months Ended September 30, 2009		Nine Months Ended September 30, 2009
Diluted net income per share				
Numerator				
Net income avilable to common shareholders		1,800,771		5,011,903
Accretion of redeemable convertible preferred stock		34,000		908,278
Net income, as adjusted	$	1,834,771	$	5,920,181
Denominator				
Weighted average common shares outstanding		22,511,824		20,109,294
Add: Options to purchase common shares		2,100,371		1,817,302
Weighted average common shares outstanding, diluted		24,612,195		21,926,596
Diluted net income per share	$	0.07	$	0.27

		Three Months Ended September 30, 2010		Nine Months Ended September 30, 2010
Basic net income per share				
Numerator				
Net income	$	3,994,531	$	15,711,756
Denominator				
Weighted average common shares outstanding, basic		23,435,172		23,072,983
Basic net income per share	$	0.17	$	0.68

		Three Months Ended September 30, 2010		Nine Months Ended September 30, 2010
Diluted net income per share				
Numerator				
Net income	$	3,994,531	$	15,711,756
Denominator				
Weighted average common shares outstanding		23,435,172		23,072,983
Add: Options to purchase common shares		1,447,595		1,661,960

Weighted average common shares outstanding, diluted		24,882,767		24,734,943
Diluted net income per share	$	0.16	$	0.64

Recently Issued Accounting Pronouncements In October 2009, an update was made to *Revenue Recognition Multiple Deliverable Revenue Arrangements.* This update removes the objective-and-reliable-evidence-of-fair-value criterion from the separation criteria used to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting, replaces references to fair value with selling price to distinguish from the fair value measurements required under the *Fair Value Measurements and Disclosures* guidance, provides a hierarchy that entities must use to estimate the selling price, eliminates the use of the residual method for allocation, and expands the ongoing disclosure requirements. This update is effective for the Company beginning January 1, 2011 and can be applied prospectively or retrospectively. Management is currently evaluating the effect that adoption of this update will have on its consolidated financial statements.

3. Fair Value of Financial Instruments

The carrying value of the Company s financial instruments, including cash equivalents, restricted cash, accounts receivable, and accounts payable, approximate their fair values due to their short maturities. The Company s financial assets and liabilities are measured using inputs from the three levels of the fair value hierarchy. A financial asset or liability s classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement. The three levels are as follows:

Level 1: Unadjusted quoted prices for identical assets or liabilities in active markets accessible by the Company at the measurement date.

Level 2: Inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3: Unobservable inputs that reflect the Company s assumptions about the assumptions that market participants would use in pricing the asset or liability.

The following table summarizes the basis used to measure certain of the Company s financial assets that are carried at fair value:

		Basis of Fair Value Measurements		
	Balance	**Quoted Prices in Active Markets for Identical Items (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Balance at December 31, 2009				
Cash equivalents money market funds	$77,947,705	$77,947,705	$	$
Cash equivalents bank deposits	5,003,453		5,003,453	
Short-term marketable securities U.S. government agency securities	29,956,204	29,956,204		
Balance at September 30, 2010				
Cash equivalents money market funds	$47,902,489	$47,902,489	$	$
Cash equivalents bank deposits	5,018,293		5,018,293	
Short-term marketable securities U.S. government agency securities	80,374,944	80,374,944		

Bank deposits are classified within the second level of the fair value hierarchy and the fair value of those assets are determined based upon quoted prices for similar assets in active markets.

4. Intangible Assets

Intangible assets consisted of the following:

December 31, 2009	September 30, 2010

	Estimated Useful Life	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Identifiable intangible assets:							
Trademark	5 years	$ 635,506	$ 436,004	$ 199,502	$ 635,506	$ 531,330	$ 104,176
Customer base	5 years	1,003,068	688,178	314,890	1,003,068	838,638	164,430
Domain names	5 years				197,991		197,991
Software	4 years	298,977	256,400	42,577	298,977	298,977	
Technology	4 years	1,361,900	1,167,954	193,946	1,361,900	1,361,900	
Internally developed software	3 years				178,647		178,647
		$ 3,299,451	$ 2,548,536	$ 750,915	$ 3,676,089	$ 3,030,845	$ 645,244

The Company is amortizing the intangible assets on a straight-line basis over the estimated useful lives noted above. Amortization expense for intangible assets was $185,734 and $110,842 for the three months ended September 30, 2009 and 2010, respectively and $557,201 and $482,309 for the nine months ended September 30, 2009 and 2010, respectively. Amortization relating to software, technology and internally developed software is recorded within cost of revenues and the amortization of trademark, customer base, and domain names is recorded within operating expenses. Future estimated amortization expense for intangible assets was as follows at September 30, 2010:

Amortization Expense (years ending December 31)	Amount
2010 (three months ending December 31)	$103,416
2011	285,824
2012	99,147
2013	84,260
2014	39,598
2015	32,999

5. Accrued Expenses

Accrued expenses consisted of the following:

	December 31, 2009	September 30, 2010
Marketing programs	$ 1,242,250	$ 2,578,540
Payroll and payroll related	3,185,126	3,747,292
Professional fees	450,788	453,543
Other accrued liabilities	2,445,012	2,104,344
Total accrued expenses	$ 7,323,176	$ 8,883,719

6. Income Taxes

The Company s tax provision for the nine months ended September 30, 2010 includes a tax benefit of $5,572,000 related to the reversal of its valuation allowance against U.S. and certain foreign deferred tax assets, which was recorded in the second quarter of 2010. The tax benefit for the nine months ended September 30, 2010 is offset by a provision for federal, state and foreign income taxes of approximately $1,989,000. The Company s tax provision for the three and nine months ended September 30, 2009 primarily consists of alternative minimum taxes, foreign income taxes and a deferred provision related to the book and tax basis differences of goodwill. The 2009 provision was substantially offset by a decrease to the valuation allowance as net loss carry-forwards were utilized to offset domestic pretax income for the period.

Deferred income taxes are provided for the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, and operating loss carry-forwards and credits using enacted tax rates expected to be in effect in the years in which the differences are expected to reverse. At each balance sheet date, the Company assesses the likelihood that deferred tax assets will be realized, and recognizes a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction. As of December 31, 2009 and March 31, 2010, the Company provided a full valuation allowance against its deferred tax assets as it believed the objective and verifiable evidence of its historical pretax net losses outweighed the positive evidence of its pre-tax income for the year ended December 31, 2009 and the three months ended March 31, 2010 and forecasted future results.

At June 30, 2010, the Company reassessed the need for a valuation allowance against its deferred tax assets and concluded that it was more likely than not that it would be able to realize certain of its deferred tax assets primarily as

a results of continued profitability and forecasted future results. Accordingly, the Company reversed its valuation allowance related to its U.S. and certain foreign deferred tax assets and recorded an income tax benefit of approximately $5,572,000 for the three months ended June 30, 2010. The release of the valuation allowance was approximately $9,077,000, of which a portion was recorded as a discrete item in the period ended June 30, 2010, and the remaining portion, which primarily relates to deferred tax assets expected to be utilized in 2010, will impact the effective income tax rate in 2010. As of September 30, 2010, the Company maintained a full valuation allowance related to the deferred tax assets of its Hungarian subsidiary.

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The Company s income tax returns since inception are open to examination by federal, state, and foreign tax authorities. The Company has no amount recorded for any unrecognized tax benefits, and its policy is to record estimated interest and penalty related to the underpayment of income taxes or unrecognized tax benefits as a component of its income tax provision. During the three and nine months ended September 30, 2009 and 2010,

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the Company did not recognize any interest or penalties in its statements of operations, and there are no accruals for interest or penalties at December 31, 2009 or September 30, 2010.

The Company has performed an analysis of its ownership changes as defined by Section 382 of the Internal Revenue Code and has determined that an ownership change as defined by Section 382 occurred in October 2004 and March 2010 resulting in approximately $219,000 and $12,133,000, respectively, of net operating losses (NOLs) being subject to limitation. As of December 31, 2009 and September 30, 2010, the Company believes all NOLs generated by the Company, including those subject to limitation, are available for utilization given the Company s large annual limitation amount.

7. Common Stock and Stockholders Equity

Public Offerings On July 7, 2009, the Company closed its IPO of 7,666,667 shares of common stock at an offering price of $16.00 per share, of which 5,750,000 shares were sold by the Company and 1,916,667 shares were sold by selling stockholders, resulting in net proceeds to the Company of approximately $83,000,000, after deducting underwriting discounts and offering costs. At the closing of the Company s IPO, all outstanding shares of redeemable convertible preferred stock were automatically converted into 12,360,523 shares of common stock.

On November 26, 2009 and December 16, 2009, the Company closed its secondary offering of an aggregate of 3,226,831 shares of common stock at an offering price of $18.50 per share, of which 99,778 shares were sold by the Company and 3,127,053 shares were sold by selling stockholders, resulting in net proceeds to the Company of $1,236,055, after deducting underwriting discounts and offering costs.

8. Stock Option Plans

On June 9, 2009, the Company s Board of Directors approved the 2009 Stock Incentive Plan (the 2009 Plan) which became effective upon the closing of the IPO. A total of 800,000 shares of common stock, subject to increase on an annual basis, were reserved for future issuance under the 2009 Plan. Shares of common stock reserved for issuance under the 2007 Stock Incentive Plan that remained available for issuance at the time of effectiveness of the 2009 Plan and any shares of common stock subject to awards under the 2007 Plan that expire, terminate, or are otherwise forfeited, canceled, or repurchased by the Company were added to the number of shares available under the 2009 Plan. The 2009 Plan is administered by the Board of Directors and Compensation Committee, which have the authority to designate participants and determine the number and type of awards to be granted, the time at which awards are exercisable, the method of payment and any other terms or conditions of the awards. Options generally vest over a four-year period and expire ten years from the date of grant. Certain options provide for accelerated vesting if there is a change in control. On January 1, 2010, subject to the provisions of the 2009 Plan, 448,996 shares were added to the shares available for grant under the 2009 Plan. On May 27, 2010, the Company s stockholders approved a 2,000,000 share increase to the shares available for grant under the 2009 Plan and removed the annual automatic share increase provision from the 2009 Plan. There were 2,367,053 shares available for grant under the 2009 Plan as of September 30, 2010.

The Company uses the Black-Scholes option-pricing model to estimate the grant date fair value of stock option grants. The Company estimates the expected volatility of its common stock at the date of grant based on the historical volatility of comparable public companies over the option s expected term as well as its own stock price volatility since the Company s IPO. The Company estimates expected term based on historical exercise activity and giving consideration to the contractual term of the options, vesting schedules, employee turnover, and expectation of employee exercise behavior. The assumed dividend yield is based upon the Company s expectation of not paying dividends in the foreseeable future. The risk-free rate for periods within the estimated life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Historical employee turnover data is used to estimate pre-vesting option forfeiture rates. The compensation expense is amortized on a straight-line basis over the requisite service period of the options, which is generally four years.

The Company used the following assumptions to apply the Black-Scholes option-pricing model:

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
	2009	2010	2009	2010

Expected dividend yield	0.00%	0.00%	0.00%	0.00%
Risk-free interest rate	2.71%	1.43%	1.88% - 2.71%	1.43% - 2.46%
Expected term (in years)	6.25	5.56 - 6.25	6.25	5.56 - 6.25
Volatility	75%	65%	75%	65% - 75%

Table of Contents

The following table summarizes stock option activity, including performance-based options:

	Number of Shares Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding, January 1, 2010	3,046,971	$ 4.90	6.8	$ 45,814,298
Granted	1,016,950	21.16		
Exercised	(1,175,237)	3.17		$ 24,620,457
Forfeited	(158,275)	13.77		
Outstanding, September 30, 2010	2,730,409	$ 11.18	7.3	$ 67,711,144
Exercisable at December 31, 2009	2,199,171	$ 3.16	6.3	$ 37,072,985
Exercisable at September 30, 2010	1,292,909	$ 4.49	5.7	$ 40,713,476

The aggregate intrinsic value was calculated based on the positive differences between the estimated fair value of the Company s common stock on December 31, 2009, of $19.95, and $35.98 per share on September 30, 2010, or at time of exercise, and the exercise price of the options.

The weighted average grant date fair value of stock options issued or modified was $11.02 per share for the year ended December 31, 2009, and $13.83 for the nine months ended September 30, 2010.

The Company recognized stock based compensation expense within the accompanying condensed consolidated statements of operations as summarized in the following table:

	Three Months Ended, September 30,		Nine Months Ended, September 30,	
	2009	2010	2009	2010
Cost of revenue	$ 8,580	$ 58,889	$ 37,745	$ 196,323
Research and development	251,333	173,722	427,192	446,840
Selling and marketing	220,780	431,177	678,751	1,043,246
General and administrative	420,446	632,541	971,834	1,849,776
	$ 901,139	$ 1,296,329	$ 2,115,522	$ 3,536,185

As of September 30, 2010, there was approximately $13,980,000 of total unrecognized share-based compensation cost, net of estimated forfeitures, related to unvested stock option grants which are expected to be recognized over a weighted average period of 2.9 years. The total unrecognized share-based compensation cost will be adjusted for future changes in estimated forfeitures.

During the three and nine months ended September 30, 2010, the Company realized a tax benefit from the exercise of stock options and recorded an excess tax benefit and an increase to additional paid-in capital of approximately $1,713,000 and $2,899,000, respectively.

Of the total stock options issued subject to the plans, certain stock options have performance-based vesting. These performance-based options granted during 2004 and 2007 were granted at-the-money, contingently vest over a period of two to four years depending upon the nature of the performance goal, and have a contractual life of ten years.

Table of Contents

The performance-based stock option activity is summarized below:

	Number of Shares Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding, January 1, 2010	642,732	$ 1.25	5.7	$ 12,019,088
Granted				
Exercised	(76,000)	1.25		1,992,616
Forfeited				
Outstanding, September 30, 2010	566,732	1.25	4.8	19,682,602
Exercisable at December 31, 2009	642,732	1.25	5.7	12,019,088
Exercisable at September 30, 2010	566,732	1.25	4.8	19,682,602

The aggregate intrinsic value was calculated based on the positive differences between the estimated fair value of the Company s common stock on December 31, 2009, of $19.95 per share, and $35.98 per share on September 30, 2010, and the exercise price of the options.

9. Commitments and Contingencies

Operating Leases The Company has operating lease agreements for offices in Massachusetts, Hungary, The Netherlands, Australia and England that expire in 2010 through 2014. The lease agreement for the Massachusetts office requires a security deposit of $125,000 in the form of a letter of credit which is collateralized by a certificate of deposit in the same amount. The lease agreement for one of the Company s Hungarian offices requires a security deposit, which totaled approximately $232,361 (170,295 Euro) at September 30, 2010. The certificate of deposit and the security deposit are classified as restricted cash. The Netherlands and Budapest, Hungary leases contain termination options which allow the Company to terminate the leases pursuant to certain lease provisions.

In July 2010, the Company amended its Massachusetts lease in order to add additional office space to its corporate headquarters. The term of the new office space began in September 2010 and extends through February 2013, the termination date of the original lease. The approximate annual lease payments for the additional office space are $330,000.

Rent expense under these leases was approximately $516,000 and $600,000 for the three months ended September 30, 2009 and 2010, respectively and approximately $1,226,000 and $1,637,000 for the nine months ended September 30, 2010. The Company records rent expense on a straight-line basis for leases with scheduled escalation clauses or free rent periods.

The Company also enters into hosting services agreements with third-party data centers and internet service providers that are subject to annual renewal. Hosting fees incurred under these arrangements aggregated approximately $439,000 and $410,000 for the three months ended September 30, 2009 and 2010, respectively and approximately $1,156,000 and $1,168,000 for the nine months ended September 30, 2010.

Future minimum lease payments under non-cancelable operating leases including one year commitments associated with the Company s hosting services arrangements are approximately as follows at September 30, 2010:

Years Ending December 31	
2010 (three months ending December 31)	$ 1,206,000
2011	3,344,000
2012	2,159,000
2013	1,073,000
2014	131,000
Total minimum lease payments	$ 7,913,000

Litigation On June 2, 2009, PB&J Software, LLC, or PB&J, filed a complaint that named the Company and four other companies as defendants in a lawsuit in the U.S. District Court for the District of Minnesota (Civil Action No. 09-cv-206-JMR/SRN). The Company received service of the complaint on July 20, 2009. The complaint alleges that the Company infringed U.S. Patent No. 7,310,736, which allegedly is owned by PB&J and has claims directed to a particular application or system for transferring or storing back-up copies of files from one computer to a second computer. On July 27, 2010, the Company and PB&J entered into a License Agreement which granted the Company a fully-paid license covering the patent at issue in the action and mutually released each party from all claims. The Company paid PB&J a one-time $65,000 licensing fee. As a result the action was dismissed by the court in August of 2010.

On September 8, 2010, 01 Communique Laboratory, Inc., or 01, filed a complaint that named the Company and one other company as defendants in a lawsuit in the U.S. District Court for the Eastern District of Virginia (Civil Action No. 1:10cv1007). The Company received service of the complaint on September 10, 2010. The complaint alleges that the Company has infringed U.S. Patent No. 6,928,479, which allegedly is owned by 01 and has claims directed to a particular application or system for providing a private communication portal from one computer to a second computer. The complaint seeks damages in an unspecified amount and injunctive relief. On October 18, 2010, 01 filed a motion for preliminary injunction seeking to enjoin the Company from making, using, selling or offering for sale certain of the Corporation s access products. The Company is investigating these allegations, believes it has meritorious defenses to the claim and intends to defend the lawsuit vigorously.

The Company is from time to time subject to various other legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these other claims cannot be predicted with certainty, management does not believe that the outcome of any of these other legal matters will have a material adverse effect on the Company s consolidated financial statements.

10. Related Party Transactions

In December 2007, the Company entered into a strategic connectivity service and marketing agreement with Intel Corporation to jointly develop a service that delivers connectivity to computers built with Intel components. Under the terms of the multi-year agreement, the Company adapted its service delivery platform, Gravity, to work with specific technology delivered with Intel hardware and software products. The agreement provides that Intel will market and sell the service to its customers. Intel pays the Company a minimum license and service fee on a quarterly basis during the multi-year term of the agreement. The Company began recognizing revenue associated with the Intel service and marketing agreement upon receipt of acceptance in the quarter ended September 30, 2008. In addition, the Company and Intel share revenue generated by the use of the service by third parties to the extent it exceeds the minimum payments. In conjunction with this agreement, Intel Capital purchased 2,222,223 shares of the Company s Series B-1 redeemable convertible preferred stock for $10,000,004, which were converted into 888,889 shares of common stock in connection with the closing of the IPO on July 7, 2009.

In September 2010, Intel notified the Company that it will terminate the connectivity service and marketing agreement effective December 2010. In accordance with the termination provisions of the agreement, Intel will not owe the Company any of the $5.0 million in fees associated with 2011, the final year of the agreement, but will pay the Company a one-time termination payment of $2.5 million.

In June 2009, the Company entered into a license, royalty and referral agreement with Intel Americas, Inc., pursuant to which the Company will pay Intel specified royalties with respect to subscriptions to its products that incorporate the Intel technology covered by the service and marketing agreement with Intel Corporation. In addition, in the event Intel refers customers to the Company under this agreement, the Company will pay Intel specified fees. This agreement expired in June 2010 in accordance with its original terms.

At December 31, 2009 and September 30, 2010, Intel owed the Company approximately $101,000 and $61,000, respectively, recorded as a non-trade receivable relating to this agreement. The Company recognized approximately $1,485,000, $1,738,000, $4,521,000 and $4,711,000 of net revenue relating to these agreements for the three and nine months ended September 30, 2009 and 2010, respectively. As of December 31, 2009, the Company had recorded approximately $2,143,000 related to this agreement as deferred revenue of which approximately $1,071,000 was classified as long term deferred revenue. As of September 30, 2010, the Company has recorded approximately $1,119,000 related to this agreement as current deferred revenue, all of which is expected to be recognized as revenue in the fourth quarter of 2010. The Company recorded operating expense relating to referral fees of approximately $0 and $23,000 relating to this agreement during the three and nine months ended September 30, 2010. Approximately $19,000 and $0 relating to the referral fees and $5,000 and $0 relating to license fees are payable to Intel as of December 31, 2009 and September 30, 2010, respectively.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the unaudited condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q and the audited consolidated financial statements and notes thereto and management s discussion and analysis of financial condition and results of operations for the year ended December 31, 2009 included in our Annual Report on Form 10-K , filed with the Securities and Exchange Commission, or SEC, on February 26, 2010. This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These statements are often identified by the use of words such as may, will, expect, believe, anticipate, intend, could, estimate, or continue, and similar expressions or variations. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in the section titled Risk Factors, set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and elsewhere in this Report. The forward-looking statements in this Quarterly Report on Form 10-Q represent our views as of the date of this Quarterly Report on Form 10-Q . We anticipate that subsequent events and developments will cause our views to change. However, while we may elect to update these forward-looking statements at some point in the future,

we have no current intention of doing so except to the extent required by applicable law. You should, therefore, not rely on these forward-looking statements as representing our views as of any date subsequent to the date of this Quarterly Report on Form 10-Q.

Overview

LogMeIn provides on-demand remote access, collaboration and support solutions to SMBs, IT service providers, mobile carries, and consumers. Businesses, carriers and IT service providers use our solutions to deliver end-user support and to remotely access and manage computers, smartphones, tablets, and other Internet-enabled devices more effectively and efficiently. Consumers and mobile workers use our solutions to remotely access PCs and Macs, thereby facilitating their mobility and increasing their productivity. SMBs and mobile professionals use our solutions to meet online and quickly collaborate on projects. Our solutions, which are deployed on-demand and accessible through a web browser, are secure, scalable and easy for our customers to try, purchase and use.

We offer three free services and ten premium services. Sales of our premium services are generated through word-of-mouth referrals, web-based advertising, expiring free trials that we convert to paid subscriptions and direct marketing to new and existing customers.

We derive our revenue principally from subscription fees from SMBs, IT service providers and consumers. The majority of our customers subscribe to our services on an annual basis. Our revenue is driven primarily by the number and type of our premium services for which our paying customers subscribe. For the nine months ended September 30, 2010, we generated revenues of $70.2 million, compared to $54.2 million for the nine months ended September 30, 2009, an increase of approximately 30%. In fiscal 2009, we generated revenues of $74.4 million.

In addition to selling our services to end users, we entered into a service and marketing agreement with Intel Corporation in December 2007 pursuant to which we have adapted our service delivery platform, Gravity, to work with specific technology delivered with Intel hardware and

software products. The agreement provides that Intel will market and sell the services to its customers. Intel pays us a minimum license and service fee on a quarterly basis during the term of the agreement, and we share with Intel revenue generated by the use of the services by third parties to the extent it exceeds the minimum payments. We began recognizing revenue associated with the Intel service and marketing agreement in the quarter ended September 30, 2008 upon receipt of customer acceptance. During the nine months ended September 30, 2010, we recognized $4.7 million in net revenue from this agreement. In September 2010, Intel notified the Company that it will terminate the connectivity service and marketing agreement effective December 2010. In accordance with the termination provisions of the agreement, Intel will not owe the Company any of the $5.0 million in fees associated with 2011, the final year of the agreement, but will pay the Company a one-time termination payment of $2.5 million.

Certain Trends and Uncertainties

The following represents a summary of certain trends and uncertainties, which could have a significant impact on our financial condition and results of operations. This summary is not intended to be a complete list of potential trends and uncertainties that could impact our business in the long or short term. The summary, however, should be considered along with the factors identified in the section titled Risk Factors set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and elsewhere in this report.

We continue to closely monitor current adverse economic conditions, particularly as they impact SMBs, IT service providers and consumers. We are unable to predict the likely duration and severity of the current adverse economic conditions in the United States and other countries, but the longer the duration the greater risks we face in operating our business.

We believe that competition will continue to increase. Increased competition could result from existing competitors or new competitors that enter the market because of the potential opportunity. We will continue to closely monitor competitive activity and respond accordingly. Increased competition could have an adverse effect on our financial condition and results of operations.

We believe that as we continue to grow revenue at expected rates, our cost of revenue and operating expenses, including sales and marketing, research and development and general and administrative expenses will increase in absolute dollar amounts. For a description of the general trends we anticipate in various expense categories, see Cost of Revenue and Operating Expenses below.

Sources of Revenue

We derive our revenue principally from subscription fees from SMBs, IT service providers and consumers. Our revenue is driven primarily by the number and type of our premium services for which our paying customers subscribe and is not concentrated within one customer or group of customers. The majority of our customers subscribe to our services on an annual basis and pay in advance, typically with a credit card, for their subscription. A smaller percentage of our customers subscribe to our services on a monthly basis through either month-to-month commitments or annual commitments that are then paid monthly with a credit card. We initially record a subscription fee as deferred revenue and then recognize it ratably, on a daily basis, over the life of the subscription period. Typically, a subscription automatically renews at the end of a subscription period unless the customer specifically terminates it prior to the end of the period.

In addition to our subscription fees, to a lesser extent, we also generate revenue from license and annual maintenance fees from the licensing of our RemotelyAnywhere product. We license RemotelyAnywhere to our customers on a perpetual basis. We do not have vendor specific objective evidence of fair value, or VSOE, for our maintenance arrangements, therefore we record the initial license and maintenance fee as deferred revenue and recognize the fees as revenue ratably, on a daily basis, over the initial maintenance period. We also initially record maintenance fees for subsequent maintenance periods as deferred revenue and recognize revenue ratably, on a daily basis, over the maintenance period. We also generate revenue from the license of our Ignition for iPhone , iPad and Android product which is sold as a perpetual license and is recognized as delivered. Revenue from RemotelyAnywhere, Ignition for iPhone, iPad and Android represented approximately 7% and 6% of our revenue for the three and nine months ended September 30, 2010, respectively.

Employees

We have increased our number of full-time employees to 387 at September 30, 2010 as compared to 338 at December 31, 2009 and 334 at September 30, 2009.

Cost of Revenue and Operating Expenses

We allocate certain overhead expenses, such as rent and utilities, to expense categories based on the headcount in or office space occupied by personnel in that expense category as a percentage of our total headcount or office space. As a result, an overhead allocation associated with these costs is reflected in the cost of revenue and each operating expense category.

Cost of Revenue. Cost of revenue consists primarily of costs associated with our data center operations and customer support centers, including wages and benefits for personnel, telecommunication and hosting fees for our services, equipment maintenance, maintenance and license fees for software licenses and depreciation. Additionally, amortization expense associated with the acquired software and technology as well as internally developed software is included in cost of revenue. The expenses related to hosting our services and supporting our free and premium customers is related to the number of customers who subscribe to our services and the complexity and redundancy of our services and hosting infrastructure. We expect these expenses to increase in absolute dollars as we continue to increase our number of customers over time but, in total, to remain relatively constant as a percentage of revenue.

Research and Development. Research and development expenses consist primarily of wages and benefits for development personnel and are generally expensed as incurred, consulting fees associated with outsourced development projects, facilities rent and depreciation associated with assets used in development. We have focused our research and development efforts on both improving ease of use and functionality of our existing services, as well as developing new offerings. The majority of our research and development employees are located in our development centers in Hungary. Therefore, a majority of research and development expense is subject to fluctuations in foreign exchange rates. During the third quarter, we capitalized approximately $180,000 of costs related to internally developed computer software to be sold as a service, which was incurred during the application development stage. No amounts were capitalized prior to the third quarter of 2010 as the costs incurred during such stage have historically been immaterial. As a result, the majority of research and development costs have been expensed as incurred. We expect that research and development expenses will increase in both absolute dollars and as a percentage of revenue as we continue to enhance and expand our services.

Sales and Marketing. Sales and marketing expenses consist primarily of online search and advertising costs, wages, commissions and benefits for sales and marketing personnel, offline marketing costs such as media advertising and trade shows, and credit card processing fees. Online search and advertising costs consist primarily of pay-per-click payments to search engines and other online advertising media such as banner ads. Offline marketing costs include radio and print advertisements as well as the costs to create and produce these advertisements, and tradeshows, including the costs of space at trade shows and costs to design and construct trade show booths. Advertising costs are expensed as incurred. In order to continue to grow our business and awareness of our services, we expect that we will continue to commit resources to our sales and marketing efforts. We expect that sales and marketing expenses will increase in absolute dollars but decrease as a percentage of revenue over time as our revenue increases.

General and Administrative. General and administrative expenses consist primarily of wages and benefits for management, human resources, internal IT support, finance and accounting personnel, professional fees, insurance and other corporate expenses. We expect that general and administrative expenses will increase as we continue to add personnel and enhance our internal information systems in connection with the growth of our business. In addition, we anticipate that we will incur additional personnel expenses, professional service fees, including auditing, legal and insurance costs. We expect that our general and administrative expenses will increase in both absolute dollars and as a percentage of revenue.

Critical Accounting Policies

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of our financial statements and related disclosures requires us to make estimates, assumptions and judgments that affect the reported amount of assets, liabilities, revenue, costs and expenses, and related disclosures. We base our estimates and assumptions on historical experience and other factors that we believe to be reasonable under the circumstances. We evaluate our estimates and assumptions on an ongoing basis. Our actual results may differ from these estimates under different assumptions and conditions. Our most critical accounting policies are listed below:

- Revenue recognition;
- Income taxes;
- Valuation of long lived and intangible assets, including goodwill; and
- Stock-based compensation.

During the three and nine months ended September 30, 2010, there were no significant changes in our critical accounting policies or estimates. See Notes 2, 6 and 8 to our condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q and included in our Annual Report on Form 10-K for the year ended December 31, 2009, as filed with the SEC on February 26, 2010, for additional information about these critical accounting policies, as well as a description of our other significant accounting policies.

Table of Contents

Results of Consolidated Operations

The following table sets forth selected consolidated statements of operations data for each of the periods indicated as a percentage of total revenue.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2010	2009	2010
Revenue	100%	100%	100%	100%
Cost of revenue	10	9	10	10
Gross profit	90	91	90	90
Operating expenses:				
Research and development	19	14	18	15
Sales and marketing	48	45	49	46
General and administrative	12	12	11	12
Amortization of intangibles			1	
Total operating expenses	79	71	77	73
Income from operations	11	20	12	17
Interest and other expense, net	(1)	1		
Income before for income taxes	10	21	12	17
Benefit (provision) for income taxes		(5)		5
Net income	10%	16%	12%	22%

Three Months Ended September 30, 2010 and 2009

Revenue. Revenue for the three months ended September 30, 2010 was $25.4 million, an increase of $6.4 million, or 34%, over revenue of $19.0 million for the three months ended September 30, 2009. Of the 34% increase in revenue, the majority of the increase was due to an increase in revenue from new customers, as our total number of premium accounts increased to approximately 490,000 at September 30, 2010 from approximately 260,000 premium accounts at September 30, 2009, and incremental add-on revenues from the our existing customer base.

Cost of Revenue. Cost of revenue for the three months ended September 30, 2010 was $2.2 million, an increase of $0.3 million, or 17%, over cost of revenue of $1.9 million for the three months ended September 30, 2009. As a percentage of revenue, cost of revenue was 9% and 10% for the three months ended September 30, 2010 and 2009, respectively. The increase in absolute dollars resulted primarily from an increase in both the number of customers using our premium services and the total number of devices that connected to our services, including devices owned by free users, which resulted in increased hosting and customer support costs. Of the increase in cost of revenue, $0.2 million resulted from increased data center costs associated with managing our data centers and the hosting of our services. The increase in data center costs was due to the expansion of our data center facilities as we added capacity to our hosting infrastructure. Additionally, $0.2 million of the increase in cost of revenue was due to the

increased costs in our customer support organization, primarily as a result of hiring new employees to support our customer growth.

Research and Development Expenses. Research and development expenses for the three months ended September 30, 2010 and 2009 were $3.6 million. As a percentage of revenue, research and development expenses were 14% and 19% for the three months ended September 30, 2010 and 2009, respectively. Research and development expenses in absolute dollars remained fairly consistent quarter over quarter. Personnel related costs increased as we hired additional employees to improve the ease of use and functionality of our existing services as well as develop new service offerings. The increase in personnel related costs was offset by the capitalization of approximately $0.2 million of application development stage costs during the three months ended September 30, 2010 and capitalized as part of intangible assets. Application development costs in periods prior to the three months ended September 30, 2010 were immaterial.

Sales and Marketing Expenses. Sales and marketing expenses for the three months ended September 30, 2010 were $11.5 million, an increase of $2.4 million, or 27%, over sales and marketing expenses of $9.1 million for the three months ended September 30, 2009. As a percentage of revenue, sales and marketing expenses were 45% and 48% for the three months ended September 30, 2010 and 2009, respectively. The increase in absolute dollars was primarily due to a $1.9 million increase in marketing program costs and a $0.5 million

increase in personnel related and recruiting costs from additional employees hired to support our growth in sales and expand our marketing efforts. The increase was also due to a $0.1 million increase in credit card processing fees.

General and Administrative Expenses. General and administrative expenses for the three months ended September 30, 2010 were $2.9 million, an increase of $0.6 million, or 24%, over general and administrative expenses of $2.3 million for the three months ended September 30, 2009. As a percentage of revenue, general and administrative expenses were 12% and 11% for the three months ended September 30, 2010 and 2009, respectively. The increase in absolute dollars was primarily due to a $0.5 million increase in personnel-related costs as we increased the number of general and administrative employees to support our overall growth.

Amortization of Intangibles. Amortization of intangibles for the three months ended September 30, 2010 and 2009 was $0.1 million and related to the value of intangible assets acquired in our July 2006 acquisition of Applied Networking, Inc.

Interest and Other (Income) Expense, Net. Interest and other (income) expense, net for the three months ended September 30, 2010 was income of approximately $0.1 million, compared to an expense of approximately $0.1 million for the three months ended September 30, 2009. The change was mainly due to an increase in interest income resulting from an increase in higher yielding marketable securities as well as a decrease in foreign currency losses.