TWITTER, INC.
Form 10-Q
May 03, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2016

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 001-36164

Twitter, Inc.

(Exact name of registrant as specified in its charter)

Delaware	20-8913779
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1355 Market Street, Suite 900

San Francisco, California 94103

(Address of principal executive offices and Zip Code)

(415) 222-9670

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES x NO ¨

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

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

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

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

The number of shares of the registrant's common stock outstanding as of April 26, 2016 was 701,897,432.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which statements involve substantial risks and uncertainties. Forward-looking statements generally relate to future events or our future financial or operating performance. In some cases, you can identify forward-looking statements because they contain words such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “target,” “projects,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative of these words or other similar terms or expressio that concern our expectations, strategy, plans or intentions. Forward-looking statements contained in this Quarterly Report on Form 10-Q include, but are not limited to, statements about:

- our ability to attract and retain users and increase the level of engagement, including ad engagement, of our users;
- our ability to develop or acquire new products, product features and services, improve our existing products and services and increase the value of our products and services;
- our business strategies, plans and priorities, including our plans for growth and refinement of our core service;
- our ability to attract advertisers to our platforms, products and services and increase the amount that advertisers spend with us;
- our expectations regarding our user growth rate and the continued usage of our mobile applications;
- our ability to increase our revenue and our revenue growth rate;
- our ability to improve user monetization, including of our logged out and syndicated audiences;
- our future financial performance, including trends in cost per ad engagement, revenue, cost of revenue, operating expenses and income taxes;
- our expectations regarding outstanding litigation;
- the effects of seasonal trends on our results of operations;
- the sufficiency of our cash and cash equivalents and cash generated from operations to meet our working capital and capital expenditure requirements;
- our ability to timely and effectively scale and adapt our existing technology and network infrastructure;
- our ability to successfully acquire and integrate companies and assets; and
- our ability to successfully enter new markets and manage our international expansion, including our ability to operate in those countries.

We caution you that the foregoing list may not contain all of the forward-looking statements made in this Quarterly Report on Form 10-Q.

You should not rely upon forward-looking statements as predictions of future events. We have based the forward-looking statements contained in this Quarterly Report on Form 10-Q primarily on our current expectations and projections about future events and trends that we believe may affect our business, financial condition, operating results, cash flows or prospects. The outcome of the events described in these forward-looking statements is subject to risks, uncertainties and other factors described in the section titled “Risk Factors” and elsewhere in this Quarterly Report on Form 10-Q. Moreover, we operate in a very competitive and rapidly changing environment. New risks and uncertainties emerge from time to time and it is not possible for us to predict all risks and uncertainties that could have an impact on the forward-looking statements contained in this Quarterly Report on Form 10-Q. We cannot assure you that the results, events and circumstances reflected in the forward-looking statements will be achieved or occur, and actual results, events or circumstances could differ materially from those described in the forward-looking statements.

The forward-looking statements made in this Quarterly Report on Form 10-Q relate only to events as of the date on which the statements are made. We undertake no obligation to update any forward-looking statements made in this Quarterly Report on Form 10-Q to reflect events or circumstances after the date of this Quarterly Report on Form 10-Q or to reflect new information or the occurrence of unanticipated events, except as required by law. We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements and you should not place undue reliance on our forward-looking statements. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or investments we may make.

NOTE REGARDING KEY METRICS

We review a number of metrics, including monthly active users, or MAUs, changes in ad engagements and changes in cost per ad engagement, to evaluate our business, measure our performance, identify trends affecting our business, formulate business plans and make strategic decisions. See the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations—Key Metrics" for a discussion of how we calculate MAUs, changes in ad engagements and changes in cost per ad engagement.

The numbers of active users presented in this Quarterly Report on Form 10-Q are based on internal company data. While these numbers are based on what we believe to be reasonable estimates for the applicable period of measurement, there are inherent challenges in measuring usage and user engagement across our large user base around the world. For example, there are a number of false or spam accounts in existence on our platform. We have performed an internal review of a sample of accounts and estimate that false or spam accounts represented less than 5% of our MAUs as of December 31, 2015. In making this determination, we applied significant judgment, so our estimation of false or spam accounts may not accurately represent the actual number of such accounts, and the actual number of false or spam accounts could be higher than we have estimated. We are continually seeking to improve our ability to estimate the total number of spam accounts and eliminate them from the calculation of our active users, and in the past have made improvements in our spam detection capabilities that have resulted in the suspension of a large number of accounts. Spam accounts that we have identified are not included in the active user numbers presented in this Quarterly Report on Form 10-Q. We treat multiple accounts held by a single person or organization as multiple users for purposes of calculating our active users because we permit people and organizations to have more than one account. Additionally, some accounts used by organizations are used by many people within the organization. As such, the calculations of our active users may not accurately reflect the actual number of people or organizations using our platform.

Our metrics are also affected by applications that automatically contact our servers for regular updates with no discernible user-initiated action involved, and this activity can cause our system to count the users associated with such applications as active users on the day or days such contact occurs. As of December 31, 2015, less than 8.5% of users used third-party applications that may have automatically contacted our servers for regular updates without any discernible additional user-initiated action. As such, the calculations of MAUs presented in this Quarterly Report on Form 10-Q may be affected as a result of this activity.

In addition, our data regarding user geographic location for purposes of reporting the geographic location of our MAUs is based on the IP address or phone number associated with the account when a user initially registered the account on Twitter. The IP address or phone number may not always accurately reflect a user's actual location at the time such user engaged with our platform.

We regularly review and may adjust our processes for calculating our internal metrics to improve their accuracy. Our measures of user growth and user engagement may differ from estimates published by third parties or from similarly-titled metrics of our competitors due to differences in methodology.

Additionally, as we previously announced, our reported MAUs will no longer include SMS fast followers; however, we will include SMS fast followers in our total audience count, as we make those disclosures. We present and discuss our total audience based on both internal metrics and relying on data from Google Analytics, which measures logged out visitors to our properties.

PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

TWITTER, INC.

CONSOLIDATED BALANCE SHEETS

(In thousands, except par value)

(Unaudited)

	March 31, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	$1,027,661	$911,471
Short-term investments	2,548,749	2,583,877
Accounts receivable, net of allowance for doubtful accounts of $7,850 and $8,121 as of March 31, 2016 and December 31, 2015, respectively	576,800	638,694
Prepaid expenses and other current assets	235,699	247,750
Total current assets	4,388,909	4,381,792
Property and equipment, net	746,713	735,299
Intangible assets	128,274	141,015
Goodwill	1,122,533	1,122,728
Other assets	89,739	61,605
Total assets	$6,476,168	$6,442,439
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$90,353	$134,081
Accrued and other current liabilities	250,720	283,792
Capital leases, short-term	81,692	88,166
Total current liabilities	422,765	506,039
Convertible notes	1,475,513	1,455,095
Capital leases, long-term	45,478	59,695
Deferred and other long-term tax liabilities, net	3,847	2,978
Other long-term liabilities	51,079	50,585
Total liabilities	1,998,682	2,074,392
Commitments and contingencies (Note 11)		
Stockholders' equity:		
Preferred stock, $0.000005 par value-- 200,000 shares authorized; none issued and outstanding	—	—
Common stock, $0.000005 par value-- 5,000,000 shares authorized; 700,203 and 694,132 shares issued and outstanding as of March 31, 2016 and December 31, 2015, respectively	3	3
Additional paid-in capital	6,681,181	6,507,087

Accumulated other comprehensive loss	(30,490)	(45,566)
Accumulated deficit	(2,173,208)	(2,093,477)
Total stockholders' equity	4,477,486	4,368,047
Total liabilities and stockholders' equity	$6,476,168	$6,442,439

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

TWITTER, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended March 31,	
	2016	2015
Revenue	$594,521	$435,939
Costs and expenses		
Cost of revenue	198,405	143,475
Research and development	155,794	189,746
Sales and marketing	236,171	183,557
General and administrative	63,267	65,777
Total costs and expenses	653,637	582,555
Loss from operations	(59,116)	(146,616)
Interest expense	(24,893)	(24,319)
Other income (expense), net	6,306	9,125
Loss before income taxes	(77,703)	(161,810)
Provision for income taxes	2,028	632
Net loss	$(79,731)	$(162,442)
Net loss per share attributable to common stockholders:		
Basic	$(0.12)	$(0.25)
Diluted	$(0.12)	$(0.25)
Weighted-average shares used to compute net loss per share attributable to common stockholders:		
Basic	691,564	640,464
Diluted	691,564	640,464

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

TWITTER, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(In thousands)

(Unaudited)

	Three Months Ended March 31,	
	2016	2015
Net loss	$(79,731)	$(162,442)
Other comprehensive income (loss):		
Unrealized gain on investments in available-for-sale securities, net of tax	4,442	570
Foreign currency translation adjustment	10,634	(33,502)
Net change in accumulated other comprehensive loss	15,076	(32,932)
Comprehensive loss	$(64,655)	$(195,374)

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

TWITTER, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Three Months Ended March 31, 2016	2015
Cash flows from operating activities		
Net loss	$(79,731)	$(162,442)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	88,621	67,864
Stock-based compensation expense	150,916	182,805
Amortization of discount on convertible notes	18,370	16,638
Changes in bad debt provision	(158)	2,792
Deferred income tax	86	(1,942)
Other adjustments	6,605	(6,411)
Changes in assets and liabilities, net of assets acquired and liabilities assumed from acquisitions:		
Accounts receivable	65,756	(4,159)
Prepaid expenses and other assets	(12,819)	(2,640)
Accounts payable	(37,033)	(1,714)
Accrued and other liabilities	(37,849)	1,390
Net cash provided by operating activities	162,764	92,181
Cash flows from investing activities		
Purchases of property and equipment	(59,148)	(67,735)
Purchases of marketable securities	(581,069)	(729,793)
Proceeds from maturities of marketable securities	595,586	712,405
Proceeds from sales of marketable securities	21,289	178,631
Changes in restricted cash	(76)	(3,362)
Business combinations, net of cash acquired	—	(28,927)
Other investing activities	(5,000)	(2,000)
Net cash provided by (used in) investing activities	(28,418)	59,219
Cash flows from financing activities		
Taxes paid related to net share settlement of equity awards	(2,124)	(6,174)
Repayments of capital lease obligations	(24,917)	(33,546)
Proceeds from exercise of stock options	2,941	3,749
Other financing activities	21	—
Net cash used in financing activities	(24,079)	(35,971)
Net increase in cash and cash equivalents	110,267	115,429
Foreign exchange effect on cash and cash equivalents	5,923	(18,748)
Cash and cash equivalents at beginning of period	911,471	1,510,724
Cash and cash equivalents at end of period	$1,027,661	$1,607,405
Supplemental disclosures of non-cash investing and financing activities		
Common stock issued in connection with acquisitions	$—	$57,679
Equipment purchases under capital leases	$4,349	$4,821

Changes in accrued property and equipment purchases	$(1,309)	$12,360

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

TWITTER, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Description of Business and Summary of Significant Accounting Policies

Twitter, Inc. (“Twitter” or the “Company”) was incorporated in Delaware in April 2007, and is headquartered in San Francisco, California. Twitter offers products and services for users, advertisers, developers and platform and data partners.

Basis of Presentation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”). The unaudited interim consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and reflect, in management’s opinion, all adjustments of a normal, recurring nature that are necessary for the fair statement of the Company’s financial position, results of operations and cash flows for the interim periods, but are not necessarily indicative of the results expected for the full fiscal year or any other period.

The accompanying interim consolidated financial statements and these related notes should be read in conjunction with the consolidated financial statements and related notes included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015.

Use of Estimates

The preparation of the Company’s consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, as well as related disclosure of contingent assets and liabilities. The Company bases its estimates on past experience and other assumptions that the Company believes are reasonable under the circumstances, and the Company evaluates these estimates on an ongoing basis. Actual results could differ materially from the Company’s estimates. To the extent that there are material differences between these estimates and actual results, the Company’s financial condition or operating results will be affected.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued a new accounting standard update on revenue recognition from contracts with customers. The new guidance will replace all current GAAP guidance on this topic and eliminate industry-specific guidance. According to the new guidance, revenue is recognized when promised goods or services are transferred to customers in an amount that reflects the consideration for which the Company expects to be entitled in exchange for those goods or services. In July 2015, the FASB decided to delay the effective date of the guidance by one year and permit early adoption for annual and interim periods beginning after December 15, 2016. As a result of the revision, the guidance will be effective for fiscal years, and interim periods with those fiscal years, beginning after December 15, 2017 and can be applied either retrospectively to each period presented or as a cumulative-effect adjustment as of the date of adoption. In March 2016 and April 2016, the FASB further amended the guidance to clarify the implementation on principal versus agent considerations, the identification of performance obligation and the licensing implementation guidance. The Company has not yet selected a transition method and is evaluating the impact of adopting these new accounting standard updates on the financial statements and related disclosures.

In June 2014, the FASB issued a new accounting standard update on stock-based compensation when the terms of an award provide that a performance target could be achieved after the requisite service period. The new guidance requires that a performance target that affects vesting, and that could be achieved after the requisite service period, be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. This update further clarifies that compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the periods for which the requisite service has already been rendered. The Company adopted this guidance prospectively during the three months ended March 31, 2016, and the adoption had no impact to the Company’s financial statements.

In February 2015, the FASB issued a new accounting standard update on consolidation analysis. The new guidance amends the current consolidation guidance with respect to the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. This guidance became effective for reporting periods beginning after December 15, 2015. The Company adopted this guidance retrospectively during the three months ended March 31, 2016, and the adoption had no impact on the Company's financial statements.

In April 2015, the FASB issued a new accounting standard update on the presentation of debt issuance costs. The new guidance requires the debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The Company adopted this guidance retrospectively during the three months ended March 31, 2016 and the adoption had an immaterial impact on the Company's financial statements.

In September 2015, the FASB issued a new accounting standard update on simplifying the accounting for measurement-period adjustments in business combinations. The new guidance requires that the adjustments to provisional amounts that are identified during the measurement period be recognized in the reporting period when the adjustments are determined. In addition, the effect on earnings of changes as a result of the change to the provisional amounts is required to be recorded in the same period's financial statements. The Company adopted this guidance prospectively on January 1, 2016, and the adoption had no impact on the Company's financial statements.

In January 2016, the FASB issued a new accounting standard update on the classification and measurement of financial instruments. The new guidance principally affects accounting standards for equity investments, financial liabilities where the fair value option has been elected, and the presentation and disclosure requirements for financial instruments. This guidance will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. Early adoption is permitted. Adoption of this new accounting standard update is not expected to have a material impact on the Company's financial statements.

In February 2016, the FASB issued a new accounting standard update on leases. The new guidance requires lessees to recognize right-of-use assets and lease liabilities for operating leases, initially measured at the present value of the lease payments, on the balance sheet. In addition, it requires lessees to recognize a single lease cost, calculated so that the cost of the lease is allocated over the lease term, generally on a straight-line basis. This guidance will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted. The Company is evaluating the impact of adopting this new accounting standard update on the financial statements and related disclosures and anticipates this new guidance will materially impact the Company's financial statements given the Company has a significant number of operating leases.

In March 2016, the FASB issued a new accounting standard update on simplifying the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The new guidance also allows an entity to account for forfeitures when they occur. This guidance will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. Early adoption is permitted. The Company is evaluating the impact of adopting this new accounting standard update on the financial statements and related disclosures.

Note 2. Cash, Cash Equivalents and Short-term Investments

Cash, cash equivalents and short-term investments consist of the following (in thousands):

	March 31,

	2016	December 31, 2015
Cash and cash equivalents:		
Cash	$242,542	$300,363
Money market funds	275,326	141,700
Corporate notes, certificates of deposit and commercial paper	509,793	469,408
Total cash and cash equivalents	$1,027,661	$911,471
Short-term investments:		
U.S. government and agency securities including treasury bills	$1,167,900	$1,156,418
Corporate notes, certificates of deposit and commercial paper	1,380,849	1,427,459
Total short-term investments	$2,548,749	$2,583,877

The contractual maturities of securities classified as available-for-sale as of March 31, 2016 were as follows (in thousands):

	March 31, 2016
Due within one year	$ 2,031,864
Due after one year through two years	516,885
Total	$ 2,548,749

The following tables summarize unrealized gains and losses related to available-for-sale securities classified as short-term investments on the Company's consolidated balance sheets (in thousands):

	March 31, 2016			
	Gross Amortized Costs	Gross Unrealized Gains	Gross Unrealized Losses	Aggregated Estimated Fair Value
U.S. government and agency securities including treasury bills	$1,167,851	$ 198	$ (149)	$1,167,900
Corporate notes, certificates of deposit and commercial paper	1,380,433	740	(324)	