STAMPS.COM INC
Form 10-Q
August 09, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 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: 000-26427

Stamps.com Inc.
(Exact name of registrant as specified in its charter)

Delaware	77-0454966
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1990 E. Grand Avenue
El Segundo, California 90245
(Address of principal executive offices, including zip code)

(310) 482-5800
(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 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 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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b 2 of the Exchange Act. (Check one):

Large accelerated filer	Accelerated filer
Non-accelerated filer (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

· As of July 31, 2016, there were 17,268,281 shares of the Registrant’s Common Stock issued and outstanding.

STAMPS.COM INC. AND SUBSIDIARIES
FORM 10-Q QUARTERLY REPORT FOR THE QUARTER ENDED JUNE 30, 2016

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

STAMPS.COM INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)

	June 30, 2016 (unaudited)	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	$ 116,273	$ 65,126
Short-term investments	6,403	8,553
Accounts receivable, net	46,081	55,052
Other current assets	10,437	8,345
Total current assets	179,194	137,076
Property and equipment, net	31,677	31,707
Goodwill	198,752	197,807
Intangible assets, net	89,368	95,950
Long-term investments	—	1,529
Deferred income taxes, net.	41,476	57,224
Other assets	6,580	7,321
Total assets	$ 547,047	$ 528,614
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 67,938	$ 60,816
Deferred revenue	5,273	4,000
Current portion of debt, net of debt issuance costs	5,298	4,267
Contingent consideration	—	63,209
Total current liabilities	78,509	132,292
Long-term debt, net of debt issuance costs	144,447	157,353
Total liabilities	222,956	289,645
Commitments and contingencies		
Stockholders' equity:		
Common stock, $.001 par value per share		
Authorized shares: 47,500 in 2016 and 2015		
Issued shares: 30,330 in 2016 and 29,463 in 2015		
Outstanding shares: 17,229 in 2016 and 16,697 in 2015	53	52
Additional paid-in capital	803,851	716,253
Treasury stock, at cost, 13,101 shares in 2016 and 12,766 in 2015	(202,420)	(172,410)
Accumulated deficit	(277,415)	(304,944)
Accumulated other comprehensive income	22	18
Total stockholders' equity	324,091	238,969

Total liabilities and stockholders’ equity	$ 547,047	$ 528,614

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

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STAMPS.COM INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
Revenues:				
Service	$72,590	$40,378	$141,696	$76,027
Product	4,851	4,270	10,406	9,013
Insurance	4,082	2,631	8,593	5,293
Customized postage	2,467	1,072	5,104	2,061
Other	23	9	51	18
Total revenues	84,013	48,360	165,850	92,412
Cost of revenues (exclusive of amortization of intangible assets, which is included in general and administrative expense):				
Service	8,857	6,695	18,151	12,966
Product	1,642	1,435	3,440	3,036
Insurance	1,266	927	2,629	1,850
Customized postage	1,955	881	4,122	1,711
Total cost of revenues	13,720	9,938	28,342	19,563
Gross profit	70,293	38,422	137,508	72,849
Operating expenses:				
Sales and marketing	20,082	12,536	41,479	26,557
Research and development	8,131	4,680	16,468	8,962
General and administrative	17,113	12,763	32,375	20,534
Contingent consideration charges	—	13,595	—	24,107
Litigation settlement	—	10,000	—	10,000
Total operating expenses	45,326	53,574	90,322	90,160
Income (loss) from operations	24,967	(15,152)	47,186	(17,311)
Interest expense	(905)	—	(1,820)	—
Interest and other income (loss), net	31	(14)	74	55
Income (loss) before income taxes	24,093	(15,166)	45,440	(17,256)
Income tax expense (benefit)	9,802	(4,735)	17,911	(5,855)
Net income (loss)	$14,291	$(10,431)	$27,529	$(11,401)
Net income (loss) per share				
Basic	$0.82	$(0.64)	$1.58	$(0.70)
Diluted	$0.79	$(0.64)	$1.49	$(0.70)
Weighted average shares outstanding				
Basic	17,384	16,402	17,370	16,280
Diluted	18,192	16,402 [1]	18,428	16,280 [1]

[1] Common equivalent shares are excluded from the diluted (loss) earnings per share calculation as their effect is anti-dilutive.

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

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STAMPS.COM INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net income (loss)	$ 14,291	$ (10,431)	$ 27,529	$ (11,401)
Other comprehensive income (loss), net of tax:				
Unrealized (loss) gain on investments	(8)	(22)	4	(14)
Comprehensive income (loss)	$ 14,283	$ (10,453)	$ 27,533	$ (11,415)

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

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STAMPS.COM INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended June 30, 2016	2015
Operating activities:		
Net income (loss)	$27,529	$(11,401)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	8,778	3,529
Stock-based compensation expense	15,933	6,043
Deferred income taxes	16,055	(6,205)
Stock option windfall tax benefit	(307)	—
Accretion of debt issuance costs	186	—
Contingent consideration	—	24,107
Changes in operating assets and liabilities, net of assets and liabilities acquired:		
Accounts receivable	8,971	(2,329)
Other current assets	(2,233)	(660)
Other assets	741	(771)
Deferred revenue	1,405	77
Accounts payable and accrued expenses	4,784	14,054
Net cash provided by operating activities	81,842	26,444
Investing activities:		
Sale of short-term investments	3,632	3,869
Purchase of short-term investments	—	(1,006)
Sale of long-term investments	66	1,075
Purchase of long-term investments	(15)	—
Acquisition of Endicia	(573)	—
Acquisition of property and equipment	(701)	(1,230)
Net cash provided by investing activities	2,409	2,708
Financing activities:		
Proceeds from short term financing obligation, net of repayments	510	1,897
Principal payments on term loan	(2,061)	—
Payment on revolving credit facility	(10,000)	—
Proceeds from exercise of stock options	7,042	5,067
Issuance of common stock under ESPP	1,108	776
Repurchase of common stock	(30,010)	—
Stock option windfall tax benefit	307	—
Net cash (used in) provided by financing activities	(33,104)	7,740
Net increase in cash and cash equivalents	51,147	36,892
Cash and cash equivalents at beginning of period	65,126	40,933
Cash and cash equivalents at end of period	$116,273	$77,825
Supplemental Information:		
Capital expenditures accrued but not paid at period end	$867	$6
Tenant improvement allowance	$676	$—

Income taxes paid	$1,560	$576
Issuance of 2015 and 2014 earn-out shares (see Note -2 “Acquisitions”)	$63,209	$9,225
Non cash adjustment of purchase price for Endicia acquisition	$372	$—

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

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STAMPS.COM INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Summary of Significant Accounting Policies

Basis of Presentation

We prepared the consolidated financial statements included herein pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with United States ("U.S.") generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to such rules and regulations. We believe that the disclosures are adequate to make the information presented not misleading. We recommend that these financial statements be read in conjunction with the audited financial statements and the notes thereto included in our latest annual report on Form 10-K for the fiscal year ended December 31, 2015, filed with the SEC on February 29, 2016.

In our opinion, these unaudited financial statements contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly our financial position as of June 30, 2016, our results of operations for the three and six months ended June 30, 2016 and our cash flows for the six months ended June 30, 2016. The results of operations for the interim period are not necessarily indicative of the results that may be expected for the year ending December 31, 2016.

Principles of Consolidation

The consolidated financial statements include the accounts of Stamps.com Inc., Auctane LLC, Interapptive, Inc., PSI Systems Inc. and PhotoStamps Inc. In June 2014, we completed our acquisition of 100% of the outstanding equity of Auctane LLC, the Texas limited liability company that operates ShipStation ("Auctane LLC" or "ShipStation") in a cash and contingent stock transaction. ShipStation, based in Austin, Texas, offers monthly subscription based e-commerce shipping software primarily under the brands ShipStation and Auctane. In August 2014, we completed our acquisition of 100% of the outstanding equity of Interapptive, Inc., a Missouri corporation, that operates ShipWorks ("Interapptive, Inc." or "ShipWorks") in a cash transaction. ShipWorks, based in St. Louis, Missouri, offers monthly subscription based e-commerce shipping software. In November 2015, we completed our acquisition of 100% of the outstanding shares of PSI Systems, Inc. ("Endicia"). Endicia, based in Palo Alto, California, is a leading provider of high volume shipping technologies and solutions for shipping with the USPS. See Note 2– "Acquisitions" for further discussion of our acquisitions.

Because 100% of the voting control of Auctane LLC, Interapptive, Inc. and PSI Systems, Inc. is held by us, we have consolidated ShipStation, ShipWorks and Endicia from the date we obtained control in the accompanying consolidated financial statements. Similarly, due to our 100% control of PhotoStamps, Inc., PhotoStamps Inc. is also consolidated in the accompanying consolidated financial statements from the date of its inception. All significant intercompany accounts and transactions have been eliminated.

Use of Estimates and Risk Management

The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates, and such differences may be material to the financial statements. Examples include estimates of loss contingencies, promotional coupon redemptions, the number of PhotoStamps retail boxes that will not be redeemed, realizability of deferred income taxes, the estimates and assumptions used to calculate stock-based compensation, the estimates and assumptions used to calculate the allocation of the purchase price related to our acquisitions, including related contingent consideration, and estimates regarding the useful lives of our building, patents and other amortizable intangible assets, and goodwill.

Contingencies and Litigation

We are subject to various routine litigation matters as a claimant and a defendant. We record any amounts recovered in these matters when received. We establish loss provisions for claims against us when the loss is both probable and can be reasonably estimated. If either or both of the criteria are not met, we assess whether there is at least a reasonable possibility that a loss, or additional losses, may have been incurred. If there is a reasonable possibility that a loss or additional loss may have been incurred for such proceedings, we disclose the estimate of the amount of loss or possible range of loss, or disclose that an estimate of loss cannot be made, as applicable.

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Fair Value of Financial Instruments

Carrying amounts of certain of our financial instruments, including cash, cash equivalents, accounts receivable and accounts payable, approximate fair value due to their short maturities. The fair values of investments are determined using quoted market prices for those securities or similar financial instruments. The fair value of our debt approximates book value.

In 2015 the fair value of the contingent consideration was determined based on a probability weighted method, which incorporated management's forecasts of financial measures and the likelihood of the financial measure targets being achieved using a series of options that replicated the pay-off structure of the earn-out, and the value of each of these options was determined using the Black-Scholes-Merton option pricing framework. Changes in the fair value of the contingent consideration obligations resulted from changes in the assumed timing and amount of revenue and expense estimates, changes in the probability of payment scenarios, changes in stock values, as well as changes in capital market conditions, which impacted the discount rate used in the fair valuation. Significant judgment was employed in determining the appropriateness of these assumptions as of the acquisition date and for each subsequent reporting period during 2015. See Note 2 – "Acquisitions" for a further description of the contingent consideration relating to ShipStation.

Property and Equipment

We account for property and equipment at cost less accumulated depreciation and amortization. We compute depreciation using the straight-line method over the estimated useful life of the asset, generally three to five years for furniture, fixtures and equipment and ten to forty years for building and building improvements. We have a policy of capitalizing expenditures that materially increase assets' useful lives and charging ordinary maintenance and repairs to operations as incurred. When property or equipment is disposed of, the cost and related accumulated depreciation and amortization are removed, and any gain or loss is included in operations.

Business Combinations

The acquisition method of accounting is used for business combinations. The results of operations of acquired businesses are included in our consolidated financial statements prospectively from the date of acquisition. The fair value of purchase consideration is allocated to the assets acquired, liabilities assumed and non-controlling interests in the acquired entity generally based on their fair value at the acquisition date. The excess of the fair value of purchase consideration over the fair value of the assets acquired, liabilities assumed and non-controlling interests in the acquired entity is recorded as goodwill. Historically the primary items that have generated goodwill include anticipated synergies between the acquired business and the Company and the acquired assembled workforce, neither of which qualifies for recognition as an intangible asset. Acquisition-related expenses are recognized in our consolidated financial statements as incurred.

Goodwill

Goodwill represents the excess of the fair value of consideration given over the fair value of the tangible assets, identifiable intangible assets and liabilities assumed in a business combination. We are required to test goodwill for impairment annually and whenever events or circumstances indicate the fair value of a reporting unit may be below its carrying value. Goodwill is reviewed for impairment annually on October 1. A reporting unit is the operating segment or a business that is one level below that operating segment. Reporting units are aggregated as a single reporting unit if they have similar economic characteristics. We are not aware of any indicators of impairment that would require an impairment analysis other than our annual impairment analysis as of June 30, 2016.

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Trademarks, Patents and Intangible Assets

Acquired trademarks, patents and other intangibles include both amortizable and non-amortizable assets and are included in intangible assets, net in the accompanying consolidated balance sheets. Intangible assets are carried at cost less accumulated amortization. Cost associated with internally developed intangible assets is typically expensed as incurred as research and development costs. Amortization of amortizable intangible assets is calculated on a straight-line basis, which is consistent with expected future cash flows.

Impairment of Long-Lived Assets and Intangible Assets

Long-lived assets including intangible assets with finite useful lives are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Intangible assets that have indefinite useful lives are not amortized but, instead, tested at least annually for impairment while intangible assets that have finite useful lives continue to be amortized over their respective useful lives.

Deferred Revenue

Our deferred revenue relates mainly to service revenue and PhotoStamps retail boxes. Deferred revenue related to our service revenue generally arises due to the timing of payment versus the provision of services for certain customers billed in advance. We previously sold PhotoStamps retail boxes to our customers through our website and selected third parties. Proceeds from the sale of our PhotoStamps retail boxes were initially recorded as a liability when received. We recorded the liability for outstanding PhotoStamps retail boxes in deferred revenue.

Revenue Recognition

We recognize revenue from product sales or services rendered, as well as commissions from advertising or sale of products by third party vendors to our customer base when the following four revenue recognition criteria are met: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the selling price is fixed or determinable, and collectability is reasonably assured.

Service revenue is primarily derived from monthly service fees and transaction related revenues from our USPS mailing and shipping services, our multi-carrier shipping services and our mailing and shipping integrations, and is recognized in the period that services are provided. Product sales, net of return allowances, are recorded when the products are shipped and title passes to customers. Sales of items, including customized postage, sold to customers are made pursuant to a sales contract that provides for transfer of both title and risk of loss upon our delivery to the carrier. Return allowances for expected product returns, which reduce product revenue, are estimated using historical experience. Commissions from the advertising or sale of products by a third party vendor to our customer base are recognized when the revenue is earned and collection is deemed probable.

Customers purchase postage through our mailing and shipping solutions. If the postage purchase funds are transferred directly from the customers to the USPS, we do not recognize revenue for this postage, as it is purchased by our customers directly from the USPS.

Customized postage revenue, which includes the face value of postage, from the sale of PhotoStamps and PictureItPostage sheets and rolls is made pursuant to a sales contract that provides for transfer of both title and risk of loss upon our delivery to the carrier and revenue is recognized at that time.Sale of PhotoStamps retail boxes are initially recorded as deferred revenue. PhotoStamps revenue related to the sale of these PhotoStamps retail boxes is subsequently recognized when either: 1) the PhotoStamps retail box is redeemed, or 2) the likelihood of the PhotoStamps retail box being redeemed is deemed remote ("breakage") and there is no legal obligation to remit the value of the unredeemed PhotoStamps retail boxes.

On a limited basis, we allow third parties to offer products and promotions to our customer base. These arrangements generally provide payment in the form of a flat fee or revenue sharing arrangements where we receive payment upon customers accessing third party products and services. During the three and six months ended June 30, 2016 and 2015 revenue from such advertising arrangements was not significant.

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We provide our customers with the opportunity to purchase parcel insurance directly through our solutions. Insurance revenue represents the gross amount charged to the customer for purchasing insurance and the related cost represents the amount paid to our insurance brokers. We recognize revenue on insurance purchases upon the ship date of the insured package.

PhotoStamps Retail Boxes

We previously sold PhotoStamps retail boxes that are redeemable for PhotoStamps on our website. The PhotoStamps retail boxes were sold through various third party retail partners. Our PhotoStamps retail boxes are not subject to administrative fees on unredeemed boxes and have no expiration date. PhotoStamps retail box sales were recorded as deferred revenue. We concluded that sufficient company-specific historical evidence existed to determine the period of time after which the likelihood of the PhotoStamps retail boxes being redeemed was remote. Based on our analysis of the redemption data, we estimate that period of time to be 60 months after the sale of our PhotoStamps retail boxes.

We recognize breakage revenue related to our PhotoStamps retail boxes utilizing the redemption recognition method. Under the redemption recognition method, we recognize breakage revenue from unredeemed retail boxes in proportion to the revenue recognized from the retail boxes that have been redeemed. Revenue from our PhotoStamps retail boxes is included in Customized postage revenue. PhotoStamps retail box breakage revenue was not significant during the three and six months ended June 30, 2016 and 2015.

Income Taxes

We account for income taxes in accordance with Financial Accounting Standards Board (“FASB”) ASC Topic No. 740, Income Taxes (“ASC 740”), which requires that deferred tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between the book and tax basis of recorded assets and liabilities. ASC 740 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some or all of the net deferred tax assets will not be realized. We record a valuation allowance to reduce our gross deferred tax assets, which are primarily comprised of U.S. Federal and State tax loss carry-forwards, to the amount that is more likely than not (a likelihood of more than 50 percent) to be realized. In order for us to realize our deferred tax assets, we must be able to generate sufficient taxable income. We evaluate the appropriateness of our deferred tax assets and related valuation allowance in accordance with ASC 740 based on all available positive and negative evidence. As of June 30, 2016 and December 31, 2015 we do not have any valuation allowance recorded to reduce our gross deferred tax assets as we believe we have met the more likely than not threshold we will realize our tax loss carry-forwards in the foreseeable future.

Short-Term Financing Obligation

We utilize short-term financing, which is separate from our debt, to fund certain company operations. Short-term financing is included in accrued expenses. As of June 30, 2016 we had $13.8 million in short-term financing obligations and $46.2 million of unused credit. As of December 31 , 2015 we had $13.3 million in short-term financing obligations and $34.2 million of unused credit.

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Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers ("ASU 2014-09") an updated standard on revenue recognition. This ASU will supersede the revenue recognition requirements in Accounting Standards Codification Topic 605, Revenue Recognition, and most industry-specific guidance. ASU 2014-09 provides enhancements to the quality and consistency of how revenue is reported while also improving comparability in the financial statements of companies reporting using US GAAP and International Financial Reporting Standards. The core principle of the new standard is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the Company expects to be entitled in exchange for those goods or services. In doing so the Company may be required to use more judgment and make more estimates than under current authoritative guidance. ASU 2014-09 will be effective for the Company in the first quarter of fiscal 2018 and may be applied on a full retrospective or modified retrospective approach. The Company is currently evaluating the impact the adoption of this standard will have on its consolidated financial statements.

In April 2015, the FASB issued guidance to help entities evaluate whether fees paid in a cloud computing arrangement include a software license. Pursuant to this guidance, when a cloud computing arrangement includes a software license, the customer accounts for the software license element of the arrangement consistent with the acquisition of other software licenses. When a cloud computing arrangement does not include a software license element, the customer accounts for the arrangement as a service contract. The prospective adoption of this guidance on January 1, 2016 did not have a material effect on the Consolidated Financial Statements.

In November 2015, the FASB issued guidance that requires deferred tax assets and liabilities to be presented as noncurrent in a classified statement of financial position. The guidance is effective beginning January 1, 2017, with early adoption permitted. The guidance can be applied prospectively or retrospectively. The Company elected to early adopt the requirements and apply them retrospectively as of December 31, 2015. The adoption resulted in the reclassification of $2.1 million of current deferred tax assets, net to noncurrent deferred tax assets, net in the Consolidated Balance Sheet as of June 30, 2015.

In February 2016, the FASB issued a new accounting standard for leases. The new standard generally requires the recognition of financing and operating lease liabilities and corresponding right-of-use assets on the balance sheet. For financing leases, a lessee recognizes amortization of the right-of-use asset as an operating expense over the lease term separately from interest on the lease liability. For operating leases, a lessee recognizes its total lease expense as an operating expense over the lease term. The amendments are effective for the Company in the first quarter of 2019 using a modified retrospective approach with early adoption permitted. The Company is currently evaluating the impact the adoption of this standard will have on its consolidated financial statements.

In March 2016, the FASB simplified certain areas of accounting for stock-based compensation, including accounting for the income tax consequences of stock-based compensation, determining the classification of awards as either equity or liabilities, classifying certain items within the statement of cash flows and introducing an accounting policy election to account for forfeitures of non-vested awards as they occur. The simplified guidance is effective for the Company in the first quarter of 2017. Depending on the area simplified, the guidance is effective either prospectively, retrospectively or using a modified retrospective approach. Early adoption is permitted. The Company is evaluating the effect of adoption on its Consolidated Financial Statements.

Subsequent Events

We are not aware of any material subsequent events or transactions that have occurred that would require recognition in the financial statements or disclosure in the notes to the financial statements, except the acquisition of ShippingEasy Group, Inc. described in Note 2 - Acquisitions to the consolidated financial statements.

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2. Acquisitions

We have accounted for all of our acquisitions under the acquisition method of accounting in accordance with the provisions of FASB ASC Topic No. 805 Business Combinations ("ASC 805").

ShippingEasy Acquisition

On June 16, 2016, we entered into a definitive agreement to acquire ShippingEasy Group, Inc. ("ShippingEasy") for approximately $55 million in cash. ShippingEasy, an Austin, Texas based company, offers web-based multi-carrier shipping software that allows online retailers and e-commerce merchants to organize, process, fulfill and ship their orders quickly and easily.

On July 1, 2016, we completed our acquisition of ShippingEasy. The net purchase price of approximately $55 million, which was subject to adjustments for changes in ShippingEasy's net working capital as of the date of the closing of the Transaction, certain transaction expenses and closing cash adjustments, was funded from current cash and investment balances. We plan for ShippingEasy to operate as a wholly owned subsidiary, led by its existing management team.

In connection with the acquisition we made performance based inducement equity awards to each the General Manager and the Chief Technology Officer of ShippingEasy. These inducement awards cover an aggregate of up to 43,567 common shares each if earnings targets for ShippingEasy are achieved over a two and one-half year period beginning July 1, 2016. The awards are subject to proration if at least 75% of the applicable target is achieved and are subject to forfeiture or acceleration based on changes in employment circumstances over the performance period. The awards are a material inducement to the General Manager and the Chief Technology Officer entering into employment agreements with Stamps.com in connection with the acquisition of ShippingEasy.

We also made inducement stock option grants for an aggregate of 62,000 shares of Stamps.com common stock to 48 new employees in connection with our acquisition of ShippingEasy. Each option vests 25% on the one year anniversary of the grant date with the remaining 75% vesting in approximately equal monthly increments over the immediately succeeding thirty-six months provided that the option holder is still employed by the Company on the vesting dates. The stock options have a ten year term and an exercise price equal to the closing price of Stamps.com common stock on the grant date of July 1, 2016. The stock options were granted as inducements material to the new employees entering into employment with Stamps.com.

ShippingEasy is not included in our financial statements as of and for the six months ended June 30, 2016 since the acquisition was subsequent to period end. The amounts for each major class of assets acquired and liabilities assumed are not disclosed due to the impractibiliy of completing the purchase price allocation before issuance of this report.

Endicia Acquisition

On March 22, 2015 we entered into a Stock Purchase Agreement (the "Stock Purchase Agreement") with Endicia, and Newell Rubbermaid Inc., a Delaware corporation ("Newell"). The Stock Purchase Agreement provided for our purchase of all of the issued and outstanding shares of common stock of Endicia from a wholly owned indirect subsidiary of Newell for an aggregate purchase price of $215 million in cash (the "Transaction"). The purchase price was subject to adjustment for changes in Endicia's net working capital as of the date of the closing of the Transaction and certain transaction expenses and closing cash adjustments. After receiving regulatory clearance, we closed the Transactionon

November 18, 2015.

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As part of the funding of our acquisition of Endicia, we entered into a credit agreement with a group of banks on November 18, 2015, which provided for a term loan of $82.5 million and a revolving credit facility with a maximum borrowing of $82.5 million (collectively, the “Credit Agreement”) to fund our acquisition of Endicia. The Credit Agreement is secured by substantially all of our assets. We funded our acquisition with cash of $56.5 million and debt from our Credit Agreement of $164.5 million, totaling $221.0 million. The $221.0 million consists of the following: 1) purchase price of $214.2 million, 2) $1.5 million of debt issuance costs and 3) the transfer of Endicia’s ending cash balance on November 17, 2015 of $5.3 million. Total debt issuance costs of $1.8 million, which includes $300,000 of costs incurred prior to closing, were recorded as debt discount and are being accreted as interest expense over the life of the Credit Agreement. Our Credit Agreement matures on November 18, 2020. As of June 30, 2016 our outstanding debt under the Credit Agreement, gross of debt issuance costs, was approximately $79.4 million under the term loan and approximately $72.0 million under the revolving credit facility. Because we have a letter of credit of approximately $510,000 relating to a facility lease, we have approximately $10.0 million of available and unused borrowings under the revolving credit facility as of June 30, 2016.

During the first quarter of 2016, we adjusted the purchase price of Endicia and related goodwill by approximately $945,000 due to certain acquisition date balance sheet adjustments and the settlement of net working capital with Newell. The total estimated purchase price of the acquired company is allocated to the assets acquired and the liabilities assumed based on their fair values. We have made significant estimates and assumptions in determining the allocation of the purchase price. The following table sets forth the final allocation of the purchase price (in thousands, except years):

	Fair Value	Fair Value	Useful Life (In Years)	Weighted Average Estimated Useful Life (In Years)
Trade accounts receivable	$ 10,247			
Other assets	771			
Property and equipment	2,798			
Goodwill	131,860			
Identifiable intangible assets:				
Trade name		$ 10,900	Indefinite	
Developed technology		26,100	9	
Customer relationship		43,200	6	
Total identifiable intangible assets	80,200			7
Accrued expenses and other liabilities	(10,212)			
Deferred revenue	(926)			
Total purchase price	$ 214,738			

Goodwill represents the excess of the fair value of consideration given over the fair value of the tangible assets, identifiable intangible assets and liabilities assumed in a business combination and the potential synergy of combining the operations of Stamps.com and Endicia. Such synergies include estimated cost reductions and enhanced sales and customer support which is expected to drive increased volume. The entire amount of goodwill recorded in this acquisition will be deducted for tax purposes ratably over a 15 year period. The identified intangible assets consist of trade name, developed technology and customer relationships. The estimated fair values of the trade name and developed technology were determined using the “relief from royalty” method. The estimated fair value of customer relationship was determined using the “excess earnings” method. The rate utilized to discount net cash flows to their present values was approximately 20% and was determined after consideration of the overall enterprise rate of return and the relative risk and importance of the assets to the generation of future cash flows. Developed technology and customer relationship will be amortized on a straight-line basis over their estimated useful lives. The amortization of acquired intangibles will be approximately $2.5 million per quarter for the remaining estimated useful lives.

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ShipWorks Acquisition

On August 29, 2014, we acquired 100% of the outstanding equity of Interapptive Inc., which operates ShipWorks, in a cash transaction. ShipWorks, based in St. Louis, Missouri, offers monthly subscription based e-commerce shipping software that provides simple, powerful and easy to use solutions for online sellers. ShipWorks solutions integrate with over 50 popular online sales and marketplaces systems including eBay, PayPal, Amazon, Yahoo! and others. ShipWorks offers multi-carrier shipping options and features including sending email notifications to buyers, updating online order status, generating reports and many more. During the fourth quarter of 2014, we adjusted the purchase price of ShipWorks by approximately $69,000.

The total purchase price for ShipWorks was approximately $22.1 million and was comprised of the following (in thousands):

	Fair Value
Cash consideration	$ 21,952
Deferred consideration	181
Total purchase price	$ 22,133

The total purchase price of the acquired company was allocated to the assets acquired and the liabilities assumed based on their fair values. We have made significant estimates and assumptions in determining the allocation of the purchase price. The following table sets forth the final allocation of the purchase price (in thousands, except years):

	Fair Value	Fair Value	Useful Life (In Years)	Weighted Average Estimated Useful Life (In Years)
Cash and cash equivalents	$ 803			
Trade accounts receivable	353			
Other assets	21			
Property and equipment	1,091			
Goodwill	16,349			
Identifiable intangible assets:				
Trademark		$ 200	6	
Developed technology		1,700	7	
Non-compete agreement		700	4	
Customer relationship		2,300	6	
Total identifiable intangible assets	4,900			6
Accrued expenses and other liabilities	(1,119)			
Deferred revenue	(265)			
Total purchase price	$ 22,133			

Goodwill represents the excess of the fair value of consideration given over the fair value of the tangible assets, identifiable intangible assets and liabilities assumed in a business combination and the potential synergy of combining the operations of Stamps.com and ShipWorks. The entire amount of goodwill recorded in this acquisition will be deducted for tax purposes ratably over a 15 year period. The identified intangible assets consist of trademarks, developed technology, non-compete agreements and customer relationships. The estimated fair values of the trademark and developed technology were determined using the "relief from royalty" method. The estimated fair value of the non-compete was determined using the "with and without" method. The estimated fair value of customer relationship was determined using the "excess earnings" method. The rate utilized to discount net cash flows to their present values was approximately 13% and was determined after consideration of the overall enterprise rate of return and the relative risk and importance of the assets to the generation of future cash flows. Trademark, developed technology, non-compete and customer relationship is amortized on a straight-line basis over their estimated useful lives. The amortization of acquired intangibles will be approximately $200,000 per quarter for the remaining estimated useful lives.

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ShipStation Acquisition and Contingent Consideration

On June 10, 2014, we acquired 100% of the outstanding equity of Auctane LLC, which operates ShipStation, in a cash and contingent stock transaction. ShipStation, based in Austin, Texas, offers monthly subscription based e-commerce shipping software primarily under the brands ShipStation and Auctane. ShipStation is a leading web-based shipping software solution that allows online retailers and e-commerce merchants to organize, process, fulfill and ship their orders quickly and easily. ShipStation supports automatic order importing from over 50 shopping carts and marketplaces, including eBay, Amazon, Shopify, Bigcommerce, Volusion, Squarespace and others. ShipStation offers multi-carrier shipping options, and automation features like custom hierarchical rules and product profiles that allow customers to easily and automatically optimize their shipping. Using ShipStation, an online retailer or e-commerce merchant can ship their orders from wherever they sell and however they ship.

The total purchase price for ShipStation was approximately $66.2 million and was comprised of the following (in thousands, except shares):

	Fair Value
Cash consideration	$ 50,000
Fair value of performance linked earn-out of up to 768,900 shares of Stamps.com common stock (contingent consideration)	16,242
Total purchase price	$ 66,242

The performance linked earn-out payment of Stamps.com shares (or contingent consideration) to former equity members of Auctane LLC was based on the achievement of certain financial measures within a future time period. There were two periods in which the earn-out payment was calculated. The first earn-out period was based on the achievement of certain financial measures during the six months ended December 31, 2014. The second earn-out period was based on the achievement of certain financial measures during the twelve months ended December 31, 2015. The range of Stamps.com shares available for the performance linked earn-out for both periods was between 576,675 to 768,900 shares provided that a minimum threshold for the financial measures was achieved. The first earn-out payment totaled 192,225 shares and was made in the first quarter of 2015. The second earn-out payment totaled 576,675 shares and was made in the first quarter of 2016. The fair value of the contingent consideration was determined at the acquisition date based on a probability weighted method, which incorporated management's forecasts of financial measures and the likelihood of the financial measure targets being achieved using a series of options that replicate the pay-off structure of the earn-out, and the value of each of these options was determined using the Black-Scholes-Merton option pricing framework.

The total purchase price of the acquired company was allocated to the assets acquired and the liabilities assumed based on their fair values. We have made significant estimates and assumptions in determining the allocation of the purchase price. The following table sets forth the final allocation of the purchase price (in thousands, except years):

	Fair Value	Fair Value	Useful Life (In Years)	Weighted Average Estimated Useful Life (In Years)
Cash and cash equivalents	$ 1,117			

Trade accounts receivable	254			
Other assets	39			
Property and equipment	187			
Goodwill	50,544			
Identifiable intangible assets:				
Trademark		$ 500	4	
Developed technology		5,300	8	
Non-compete agreement		400	4	
Customer relationship		9,000	8	
Total identifiable intangible assets	15,200			8
Accrued expenses and other liabilities	(835)			
Deferred revenue	(264)			
Total purchase price	$ 66,242			

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Goodwill represents the excess of the fair value of consideration given over the fair value of the tangible assets, identifiable intangible assets and liabilities assumed in a business combination and the potential synergy of combining the operations of Stamps.com and ShipStation. The entire amount of goodwill recorded in this acquisition will be deducted for tax purposes ratably over a 15 year period. The identified intangible assets consist of trademarks, developed technology, non-compete agreements and customer relationships. The estimated fair values of the trademark and developed technology were determined using the "relief from royalty" method. The estimated fair value of the non-compete was determined using the "with and without" method. The estimated fair value of customer relationship was determined using the "excess earnings" method. The rate utilized to discount net cash flows to their present values was approximately 15% and was determined after consideration of the overall enterprise rate of return and the relative risk and importance of the assets to the generation of future cash flows. Trademark, developed technology, non-compete and customer relationship is amortized on a straight-line basis over their estimated useful lives. The amortization of acquired intangibles will be approximately $500,000 per quarter for the remaining estimated useful lives.

Under ASC 805, we are required to re-measure the fair value of the contingent consideration at each reporting period. During the 2015 periods, the fair value of the contingent consideration was determined based on a probability weighted method, which incorporated management's forecasts of financial measures and the likelihood of the financial measure targets being achieved using a series of options that replicate the pay-off structure of the earn-out, and the value of each of these options was determined using the Black-Scholes-Merton option pricing framework. Increases or decreases in the fair value of the contingent consideration can result from changes in the assumed timing and amount of revenue and expense estimates, changes in the probability of payment scenarios, changes in stock values, as well as changes in capital market conditions, which impact the discount rate used in the fair valuation. Significant judgment was employed in determining the appropriateness of these assumptions as of the acquisition date and for each subsequent reporting period. We recognized $13.6 million and $24.1 million of contingent consideration charges during the three and six months ended June 30, 2015, respectively. As of December 31, 2015, the fair value of the contingent consideration was calculated by multiplying the expected earn-out shares to be distributed by our stock price at December 31, 2015. The fair value of the contingent consideration for the ShipStation acquisition was $63.2 million as of December 31, 2015, the final measurement date. No increases or decreases to the fair value of the contingent consideration were made following December 31, 2015 and prior to the second and final earn-out payment in the first quarter of 2016.

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3. Commitments and Contingencies

Legal Proceedings

We are subject to various routine legal proceedings and claims incidental to our business, and we do not believe that these proceedings and claims would reasonably be expected to have a material adverse effect on our financial position, results of operations or cash flows.

Although management at present believes that the ultimate outcome of the various routine proceedings, individually and in the aggregate, will not materially harm our financial position, results of operations, cash flows, or overall trends, legal proceedings are subject to inherent uncertainties, and unfavorable rulings or other events could occur. An unfavorable outcome for an amount in excess of management's present beliefs may result in a material adverse impact on our business, results of operations, financial position, and overall trends.

Commitments

The following table is a schedule of our significant contractual obligations and commercial commitments (other than debt commitments), which consist only of future minimum lease payments under operating leases as of June 30, 2016 (in thousands):

Twelve Month Period Ending June 30,		Operating Lease Obligation
2017	$	$ 3,118
2018		3,180
2019		1,515
2020		613
2021		572
Total		$ 8,998

4. Net Income (loss) per Share

Net income (loss) per share represents net income (loss) attributable to common stockholders divided by the weighted average number of common shares outstanding during a reporting period. The diluted net income (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock, including stock options (commonly and hereafter referred to as "common stock equivalents"), were exercised or converted into common stock. Diluted net income per share is calculated by dividing net income during a reporting period by the sum of the weighted average number of common shares outstanding plus common stock equivalents for the period.

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The following table reconciles share amounts utilized to calculate basic and diluted net income (loss) per share (in thousands, except per share data):

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
Net income (loss)	$ 14,291	$ (10,431)	$ 27,529	$ (11,401)
Basic - weighted average common shares	17,384	16,402	17,370	16,280
Diluted effect of common stock equivalents	808	— (1)	1,058	— (1)
Diluted - weighted average common shares	18,192	16,402	18,428	16,280
Earnings (loss) per share:				
Basic	$ 0.82	$ (0.64)	$ 1.58	$ (0.70)
Diluted	$ 0.79	$ (0.64)	$ 1.49	$ (0.70)

(1) Common equivalent shares are excluded from the diluted net loss per share calculation as their effect is anti-dilutive.

The calculation of dilutive shares excludes the effect of the following options that are considered anti-dilutive (in thousands):

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
Anti-dilutive stock option shares	287	2,992	147	2,978

5. Stock-Based Employee Compensation

We estimate the fair value of share-based payment awards on the date of grant using an option-pricing model and recognize stock-based compensation expense during each period based on the value of that portion of share-based payment awards that is ultimately expected to vest during the period, reduced for estimated forfeitures. We estimate forfeitures at the time of grant based on historical data and revise, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Compensation expense recognized for all employee stock options granted is recognized using the straight-line method over their respective vesting periods of up to five years.

The following table sets forth the stock-based compensation expense that we recognized for the periods indicated (in thousands):

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
Stock-based compensation expense relating to:				
Employee and director stock options	$ 8,154	$ 3,274	$ 15,435	$ 5,802
Employee stock purchases	263	127	498	241
Total stock-based compensation expense	$ 8,417	$ 3,401	$ 15,933	$ 6,043

Stock-based compensation expense relating to:				
Cost of revenues	$ 450	$ 201	$ 875	$ 368
Sales and marketing	1,857	853	3,588	1,575
Research and development	1,425	617	2,780	1,165
General and administrative	4,685	1,730	8,690	2,935
Total stock-based compensation expense	$ 8,417	$ 3,401	$ 15,933	$ 6,043

We use the Black-Scholes-Merton option valuation model to estimate the fair value of share-based payment awards on the date of grant, which requires us to make a number of highly complex and subjective assumptions, including stock price volatility, expected term, risk-free interest rates and projected employee stock option exercise behaviors. In the case of options we grant, our assumption of expected volatility is based on the historical volatility of our stock price over the term equal to the expected life of the options. We base the risk-free interest rate on U.S. Treasury zero-coupon issues with a remaining term equal to the expected life of the options assumed at the date of grant. The estimated expected life represents the weighted-average period the stock options are expected to remain outstanding, determined based on an analysis of historical exercise behavior.

The following are the weighted average assumptions used in the Black-Scholes valuation model for the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Expected dividend yield	—	—	—	—
Risk-free interest rate	1.0%	0.9%	1.0%	1.0%
Expected volatility	49%	45%	48%	46%
Expected life (in years)	3.4	3.4	3.4	3.4
Expected forfeiture rate	6%	6%	6%	6%

6. Goodwill and Intangible Assets

Goodwill represents the excess of the fair value of consideration given over the fair value of the tangible assets, identifiable intangible assets and liabilities assumed in a business combination.

The following table summarizes goodwill as of December 31, 2015 and June 30, 2016 (in thousands):

	2016
Goodwill balance at December 31, 2015	$197,807
Acquisitions (see Note 2– “Acquisitions”)	945
Goodwill balance at June 30, 2016	$198,752

Goodwill is reviewed for impairment annually on October 1st utilizing a qualitative assessment or a two-step process. We have an option to make a qualitative assessment of a reporting unit's goodwill for impairment. If we choose to perform a qualitative assessment and determine the fair value more likely than not exceeds the carrying value, no further evaluation is necessary. For reporting units where we perform the two-step process, the first step requires us to compare the fair value of each reporting unit, which we primarily determine using an income approach based on the present value of discounted cash flows, to the respective carrying value, which includes goodwill. If the fair value of the reporting unit exceeds its carrying value, the goodwill is not considered impaired. If the carrying value is higher than the fair value, there is an indication that impairment may exist and the second step is required. In step two, the implied fair value of goodwill is calculated as the excess of the fair value of a reporting unit over the fair values assigned to its assets and liabilities. If the implied fair value of goodwill is less than the carrying value of the reporting unit's goodwill, the difference is recognized as an impairment loss.

We have amortizable and non-amortizable intangible assets consisting of patents, trademarks, trade names, lease-in-place intangible assets, developed technology, non-compete agreements and customer relationships totaling approximately $109.7 million in gross carrying amount as of June 30, 2016 and December 31, 2015.

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The following table summarizes our amortizable intangible assets as of June 30, 2016 (in thousands):