

NETSCOUT SYSTEMS INC
Form 10-Q
August 07, 2007
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 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, 2007

OR

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

For the transition period from _____ to _____

Commission file number 0000-26251

NETSCOUT SYSTEMS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

310 Littleton Road, Westford, MA 01886

(978) 614-4000

04-2837575
(IRS Employer
Identification No.)

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

Indicate by check mark whether the registrant is large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

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

The number of shares outstanding of the registrant's common stock, par value \$0.001 per share, as of August 6, 2007 was 32,300,766.

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NETSCOUT SYSTEMS, INC.

FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2007

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Table of Contents**PART I: FINANCIAL INFORMATION****Item 1. Unaudited Financial Statements****NetScout Systems, Inc.****Condensed Consolidated Balance Sheets****(In thousands, except share and per share data)****(Unaudited)**

	June 30, 2007	March 31, 2007
Assets		
Current assets:		
Cash and cash equivalents	\$ 12,650	\$ 18,925
Marketable securities	80,530	69,204
Accounts receivable, net of allowance for doubtful accounts of \$20 and \$9 at June 30, 2007 and March 31, 2007, respectively	15,894	18,317
Inventories	4,932	4,562
Refundable income taxes	284	657
Deferred income taxes	2,679	2,535
Prepaid expenses and other current assets	3,401	3,380
Total current assets	120,370	117,580
Fixed assets, net	8,868	8,262
Goodwill	36,561	36,561
Acquired intangible assets, net	331	442
Capitalized software development costs, net	129	170
Deferred income taxes	5,391	5,382
Long-term marketable securities	12,035	11,975
Other assets	100	47
Total assets	\$ 183,785	\$ 180,419
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 2,973	\$ 3,023
Accrued compensation	8,011	8,271
Accrued other liabilities	2,467	2,609
Income taxes payable	809	192
Deferred revenue	24,234	23,992
Total current liabilities	38,494	38,087
Other long-term liabilities	1,007	1,008
Accrued long-term retirement benefits	1,235	1,155
Long-term deferred revenue	1,332	1,762
Total liabilities	42,068	42,012

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Commitments and contingencies (Note 7)		
Stockholders' equity:		
Preferred stock, \$0.001 par value:		
5,000,000 shares authorized; no shares issued or outstanding at June 30, 2007 and March 31, 2007		
Common stock, \$0.001 par value: 150,000,000 shares authorized; 36,733,642 and 36,581,852 shares issued and 32,201,625 and 32,049,835 shares outstanding at June 30, 2007 and March 31, 2007, respectively		
	37	36
Additional paid-in capital	122,720	122,074
Accumulated other comprehensive loss	(63)	(46)
Treasury stock at cost, 4,532,017 shares at June 30, 2007 and March 31, 2007	(28,939)	(28,939)
Retained earnings	47,962	45,282
Total stockholders' equity	141,717	138,407
Total liabilities and stockholders' equity	\$ 183,785	\$ 180,419

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

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NetScout Systems, Inc.

Condensed Consolidated Statements of Operations

(In thousands, except per share data)

(Unaudited)

	Three Months Ended June 30,	
	2007	2006
Revenue:		
Product	\$ 17,512	\$ 14,227
Service	10,400	9,348
Total revenue	27,912	23,575
Cost of revenue:		
Product (1)	4,652	3,856
Service (1)	1,487	1,267
Total cost of revenue	6,139	5,123
Gross profit	21,773	18,452
Operating expenses:		
Research and development (1)	4,534	4,422
Sales and marketing (1)	11,541	10,830
General and administrative (1)	2,833	2,106
Amortization of acquired intangible assets	6	39
Total operating expenses	18,914	17,397
Income from operations	2,859	1,055
Interest and other income, net:		
Interest income	1,018	1,025
Interest expense	(9)	(13)
Other income, net		3
Total interest and other income, net	1,009	1,015
Income before income tax expense and cumulative effect of accounting change	3,868	2,070
Income tax expense	1,188	766
Income before cumulative effect of accounting change	2,680	1,304
Cumulative effect of accounting change, net of taxes of \$41		70
Net income	\$ 2,680	\$ 1,374
Basic net income per share	\$ 0.08	\$ 0.04
Diluted net income per share	\$ 0.08	\$ 0.04
Shares used in computing:		

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Basic net income per share	32,140	31,480
Diluted net income per share	33,253	33,049

(1) Share-based compensation expenses included in these amounts are as follows:

Cost of product revenue	\$ 11	\$ 9
Cost of service revenue	12	13
Research and development	114	133
Sales and marketing	171	157
General and administrative	77	75

Total share-based compensation expense, before income tax effect	\$ 385	\$ 387
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The accompanying notes are an integral part of these condensed consolidated financial statements.

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NetScout Systems, Inc.

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Three Months Ended	
	2007	June 30, 2006
Cash flows from operating activities:		
Net income	\$ 2,680	\$ 1,374
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	884	856
Loss on disposal of fixed assets	8	17
Share-based compensation expense associated with equity awards	385	387
Cumulative effect of accounting change		(111)
Deferred income taxes	(153)	145
Changes in assets and liabilities		
Accounts receivable	2,423	1,744
Inventories	(370)	(1,570)
Refundable income taxes	373	783
Prepaid expenses and other current assets	(28)	161
Other assets	(53)	3
Accounts payable	(50)	(258)
Accrued compensation and other expenses	(323)	(1,385)
Income taxes payable	617	467
Deferred revenue	(188)	14
Net cash provided by operating activities	6,205	2,627
Cash flows from investing activities:		
Purchase of marketable securities	(13,011)	(17,622)
Proceeds from maturity of marketable securities	1,615	4,613
Purchase of fixed assets	(981)	(474)
Capitalized expenditures for internal use software	(365)	(402)
Capitalized software development costs		(15)
Net cash used in investing activities	(12,742)	(13,900)
Cash flows from financing activities:		
Proceeds from issuance of common stock	231	1,485
Tax benefit from stock options exercised	31	111
Net cash provided by financing activities	262	1,596
Net decrease in cash and cash equivalents	(6,275)	(9,677)
Cash and cash equivalents, beginning of period	18,925	61,676
Cash and cash equivalents, end of period	\$ 12,650	\$ 51,999

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

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NetScout Systems, Inc.

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Basis of Presentation

The accompanying unaudited interim condensed consolidated financial statements as of June 30, 2007 and for the three months ended June 30, 2007 and 2006, respectively, have been prepared by NetScout Systems, Inc. (NetScout or the Company) in accordance with generally accepted accounting principles for interim financial reports and the instructions for Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared under generally accepted accounting principles have been condensed or omitted pursuant to such regulations. In the opinion of the Company's management, the unaudited interim condensed consolidated financial statements include all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the Company's financial position, results of operations and cash flows. The results of operations for the three months ended June 30, 2007 are not necessarily indicative of the results of operations for the year ending March 31, 2008. The balance sheet at March 31, 2007 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2007, as filed with the Securities and Exchange Commission (SEC) on June 4, 2007.

2. Share-Based Compensation

The 1999 Stock Option Plan permits the granting of stock options, restricted stock and restricted stock units, collectively referred to as share-based awards. Periodically, the Company grants share-based awards to employees and officers of the Company. The Company accounts for these share-based awards in accordance with Statement of Financial Accounting Standards (SFAS) No. 123R, Share-Based Payment (SFAS 123R) which requires the measurement and recognition of compensation expense based on estimated fair values for all share-based payment awards made to our employees and directors. Share-based award grants are generally measured at fair value on the date of grant based on the number of shares granted and the quoted price of the Company's common stock. Such value is recognized as a cost of revenue or an operating expense over the corresponding vesting period. During the three months ended June 30, 2007 and 2006, share-based compensation expense was \$385 thousand and \$387 thousand, respectively.

The Company adopted SFAS 123R using the modified prospective transition method beginning April 1, 2006. Accordingly, the Company recorded share-based compensation expense for awards granted prior to but not yet vested as of April 1, 2006 as if the fair value method required for pro forma disclosure under SFAS 123 were in effect for expense recognition purposes, but adjusted for estimated forfeitures. The Company recorded a pre-tax cumulative benefit of accounting change of \$111 related to estimating forfeitures for share-based awards that were unvested as of April 1, 2006.

Table of Contents**NetScout Systems, Inc.****Notes to Condensed Consolidated Financial Statements (Continued)****(Unaudited)****3. Cash, Cash Equivalents and Marketable Securities**

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents and those investments with original maturities greater than three months to be marketable securities. Cash equivalents and short-term marketable securities are stated at cost plus accrued interest, which approximates fair value. Long-term marketable securities are stated at fair value based on quoted market prices. Cash equivalents and marketable securities consist primarily of money market instruments, U.S. Treasury bills and municipal obligations.

Marketable Securities

The following is a summary of marketable securities held by NetScout at June 30, 2007, with maturity dates of July 2007 through March 2009 (in thousands):

	Amortized Costs	Unrealized Losses	Fair Value
U.S. government and municipal obligations	\$ 93,739	\$ (63)	\$ 93,676
Less: restricted investment	1,132	(21)	1,111
Marketable securities	\$ 92,607	\$	