RAINING DATA CORP
Form 10QSB
August 03, 2004

U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-QSB

(Mark One)

ý	**Quarterly Report under Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended June 30, 2004

o	**Transition Report Pursuant to Section 13 or 15(d) of the Exchange Act**

For the transition period from to

Commission File number 0-16449

RAINING DATA CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**94-3046892**
(State of Incorporation)	(IRS Employer Identification No.)

17500 Cartwright Road
Irvine, CA 92614
(Address of principal executive offices)

(949) 442-4400
(Registrant s telephone number)

Check whether the issuer: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 ý No o

As of June 30, 2004, there were 18,428,141 shares of registrant s Common Stock, $.10 par value, outstanding.

Transitional Small Business Disclosure Format (Check one): Yes o No ý

RAINING DATA CORPORATION

INDEX

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

RAINING DATA CORPORATION AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2004	March 31, 2004
	(In thousands)	
ASSETS		
Current assets		
Cash	$ 8,344	$ 7,783
Trade accounts receivable-net	1,499	1,865
Other current assets	303	390
Total current assets	10,146	10,038
Property, furniture and equipment-net	742	795
Intangible assets-net	1,083	1,733
Goodwill	27,684	27,684
Other assets	180	201
Total assets	$ 39,835	$ 40,451
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities		
Accounts payable	$ 270	$ 242
Accrued liabilities	1,622	2,257
Deferred revenue	5,220	5,006
Note payable	22	38
Total current liabilities	7,134	7,543
Long term debt-net of discount	23,431	23,117
Total liabilities	30,565	30,660
Commitments and contingencies		
Stockholders equity		
Preferred stock	300	300
Common stock	1,843	1,840
Additional paid-in capital	95,472	95,418
Deferred stock-based compensation	(33)	(41)
Accumulated other comprehensive income	1,302	1,509
Accumulated deficit	(89,614)	(89,235)
Total stockholders equity	9,270	9,791
Total liabilities and stockholders equity	$ 39,835	$ 40,451

See accompanying condensed notes to the unaudited condensed consolidated financial statements.

RAINING DATA CORPORATION AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
THREE MONTHS ENDED JUNE 30,

	2004	2003
Net revenues		
Licenses	$ 2,222	$ 2,286
Services	2,975	3,123
Total net revenues	5,197	5,409
Costs of revenues		
Cost of license revenues	72	89
Cost of service revenues	468	489
Total cost of revenues	540	578
Gross profit	4,657	4,831
Cost of operations		
Selling and marketing	1,414	1,457
Research and development	1,738	1,974
General and administrative	889	920
Stock-based compensation	32	50
Amortization of intangible assets	650	650
Total operating expenses	4,723	5,051
Operating loss	(66)	(220)
Other expense		
Interest expense-net	(303)	(296)
Other income (expense)-net	(10)	16
	(313)	(280)
Net loss	$ (379)	$ (500)
Basic and diluted loss per share	$ (0.02)	$ (0.03)
Shares used in computing basic and diluted loss per share	18,415	17,956
<u>Departmental allocation of stock-based compensation</u>		
Cost of service revenues	$	$ 3
Selling and marketing expense		16
Research and development expense	30	28
General and administrative expense	2	3
Total stock-based compensation	$ 32	$ 50

See accompanying condensed notes to the unaudited condensed consolidated financial statements.

RAINING DATA CORPORATION AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

THREE MONTHS ENDED JUNE 30,

	2004	2003
	(In thousands)	
Cash flows from operating activities:		
Net loss	$ (379)	$ (500)
Adjustments to reconcile net loss to net cash provided by (used for) operating activities:		
Depreciation and amortization of long-lived assets	725	741
Note discount amortization	21	21
Amortization of deferred stock-based compensation	32	50
Change in assets and liabilities:		
Trade accounts receivable	398	119
Other current and non-current assets	86	36
Accounts payable and accrued liabilities	(602)	(912)
Deferred revenue	284	32
Net cash provided by (used for) operating activities	565	(413)
Cash flows from investing activities:		
Purchase of property, furniture and equipment - net	(7)	(1)
Net cash used for investing activities	(7)	(1)
Cash flows from financing activities:		
Proceeds from exercise of stock options and warrants	32	44
Proceeds from issuance of common stock		278
Repayment of debt	(16)	(272)
Net cash provided by financing activities	16	50
Effect of exchange rate changes on cash	(13)	34
Net increase (decrease) in cash and equivalents	561	(330)
Cash and equivalents at beginning of period	7,783	5,279
Cash and equivalents at end of period	$ 8,344	$ 4,949
Other non-cash activities:		
Issuance of payment-in-kind notes for accrued interest	$ 289	$ 182

See accompanying condensed notes to the unaudited condensed consolidated financial statements.

RAINING DATA CORPORATION AND SUBSIDIARIES

CONDENSED NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2004 (Unaudited)

1. INTERIM FINANCIAL STATEMENTS

The unaudited interim condensed consolidated financial information furnished herein reflects all adjustments, consisting only of normal recurring items, which in the opinion of management are necessary to fairly state Raining Data Corporation s (the Company) financial position, the results of its operations and its cash flows for the dates and periods presented and to make such information presented not misleading. Certain information and footnote disclosures, normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been omitted pursuant to SEC rules and regulations; nevertheless, management of the Company believes that the disclosures herein are adequate to make the information presented not misleading. These condensed consolidated financial statements should be read in conjunction with the Company s audited financial statements for the year ended March 31, 2004, contained in the Company s Annual Report on Form 10-KSB. The results of operations for the period ended June 30, 2004, are not necessarily indicative of results to be expected for any other interim period or the fiscal year ending March 31, 2005.

Stock Options

Pro forma information, which assumes the Company had accounted for stock options granted under the fair value method prescribed by Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-based Compensation, is presented below. The per share weighted-average fair values of stock options granted for the three month periods ended June 30, 2004 and 2003, as estimated using the Black-Scholes option-pricing model were $2.83 and $1.50, respectively. The following assumptions were used for the three-month period ended June 30, 2004: dividend yield of 0%; expected volatility of 126%; risk-free interest rate of 4.18%; and expected life of 7 years. The following assumptions were used for the three-month period ended June 30, 2003: dividend yield of 0%; expected volatility of 142%; risk-free interest rate of 3.13%; and expected life of 7 years.

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options vesting periods. The Company s historical and pro forma net loss per share for the three month periods ended June 30, 2004 and 2003 are as follows (in thousands, except per share data):

	Three Months ended June 30, 2004		Three Months ended June 30, 2003	
Net loss:				
As reported	$	(379)	$	(500)
Add:				
Stock-based employee compensation expense included in net loss		32		50
Less:				

Total stock-based employee compensation expense determined under the fair value method for all awards		(290)		(492)
Pro forma net loss:	$	(637)	$	(942)
Basic and diluted loss per share				
As reported	$	(0.02)	$	(0.03)
Pro forma	$	(0.03)	$	(0.05)

Reclassifications

Certain reclassifications have been made to prior period amounts to conform to the current period presentation.

2. LONG-TERM DEBT

Long-term debt of the Company, including the Convertible Subordinated Note payable to Astoria Capital Partners, L.P. (Astoria), the Company s controlling stockholder, as of June 30, 2004 and March 31, 2004, is as follows (in thousands):

RAINING DATA CORPORATION AND SUBSIDIARIES
LONG-TERM DEBT SCHEDULE

	June 30, 2004	March 31, 2004
Subordinated Convertible Note payable to Astoria	$ 23,462	$ 23,172
Plus accrued interest	292	289
Less unamortized discount	(323)	(344)
	23,431	23,117
Other long-term liabilities	22	38
Total debt	23,453	23,155
Less current portion of long-term debt	(22)	(38)
Total long-term debt	$ 23,431	$ 23,117

3. STOCKHOLDERS EQUITY

Basic loss per share is computed using the net loss and the weighted average number of common shares outstanding during the period. Diluted loss per share is computed using the net loss and the weighted average number of common shares and dilutive potential common shares outstanding during the period when the potential common shares are not anti-dilutive. Potential dilutive common shares include outstanding stock options and warrants, convertible debt, and convertible preferred stock. There were 4,053,346 and 4,027,935 outstanding options to purchase shares of the Company s common stock with exercise prices ranging from $0.75 to $52.50 per share as of June 30, 2004 and 2003, respectively. There were 2,169,647 and 2,637,086 outstanding warrants to purchase shares of the Company s common stock with exercise prices ranging from $2.35 to $6.29 and $2.35 to $6.51 per share at June 30, 2004 and 2003, respectively. There were 300,000 shares of preferred stock, which are convertible into 500,100 shares of common stock, outstanding at June 30, 2004 and 2003. There was convertible debt outstanding at June 30, 2004 and 2003, which was convertible into 4,692,407 and 4,464,335 shares of common stock, respectively. The total of these items were not included in the computation of diluted earnings per share because their effect would have been anti-dilutive.

The change in accumulated other comprehensive income during the three-month periods ended June 30, 2004 and 2003, is the result of the effect of foreign exchange rate changes. The following table reconciles net loss as reported with total comprehensive loss (in thousands):

	Three Months ended June 30, 2004		Three Months ended June 30, 2003	
Net loss reported	$	(379)	$	(500)
Translation adjustments net		(207)		122
Total comprehensive loss	$	(586)	$	(378)

4. BUSINESS SEGMENT

The Company operates in one reportable segment. International operations consist primarily of foreign sales offices selling software developed by or for the Company s entities in the United States of America, combined with local service revenue. The following table summarizes consolidated financial information of the Company s operations by geographic location (in thousands):

	North America	Europe	Total
Three Months Ended June 30, 2004			
Net revenues	$ 3,724	$ 1,473	$ 5,197
Long lived assets	29,050	639	29,689
Three Months Ended June 30, 2003			
Net revenues	$ 3,911	$ 1,498	$ 5,409
Long lived assets	31,788	655	32,443

The Company is engaged in the design, development, sale and support of software infrastructure. The Company divides its products into two main categories: (1) Pick-based database technology (Databases), which includes Multi-dimensional Database Management Systems, XML Data Management Servers and the Pick Data Provider for the Microsoft .NET development environment; and (2) Rapid Application Development software tools (RAD Tools). The following table represents the net revenue from the Company s segment by product line (in thousands):

		2004		2003
Three Months Ended June 30, 2004				
Databases	$	3,974	$	4,240
RAD Tools		1,223		1,169
Total Net Revenues	$	5,197	$	5,409

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Form 10-QSB 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. Such statements include our expectations, hopes and intentions regarding the future, including but not limited to statements regarding (i) our strategy, (ii) our research and development plans, (iii) our expectation about selling and marketing costs and general and administrative costs, (iv) the sufficiency of our capital resources, (v) our capital expenditures, (vi) our financing plan, (vii) our revenue and cost of license and service revenue, (viii) our operations and operating results, (ix) our competitive position, (x) our expectation about certain markets, and (xi) our expectation about future expenses. Forward-looking statements involve certain risks and uncertainties, and actual results may differ materially from those discussed in any such statement. Factors that could cause actual results to differ materially from such forward-looking statements include the risks described in the Risk Factors section and elsewhere in this Form 10-QSB. All forward-looking statements in this document are made as of the date hereof, based on information available to us as of the date hereof, and we assume no obligation to update any forward-looking statement.

This discussion and analysis of the financial statements and results of operations should be read in conjunction with our unaudited condensed consolidated financial statements, including the related notes thereto, contained elsewhere in this Form 10-QSB.

OVERVIEW

We were incorporated in the State of Delaware in August 1987. We were originally incorporated as Blyth Holdings, Inc., and our name was changed to Omnis Technology Corporation in September 1997. Effective December 1, 2000, we completed the acquisition of PickAx, Inc., a Delaware corporation (PickAx). Concurrent with the acquisition, we changed our name to Raining Data Corporation.

Our principal business is the design, development, sale and support of software infrastructure. Our products allow customers to create and enhance flexible software applications for their own needs and our software may be categorized into four product lines: Multi-dimensional database management systems (MDMS), XML data management servers (XDMS), the Pick Data Provider (PDP) for the Microsoft .NET development environment and Rapid Application Development (RAD) software tools.

Many of our products are based on the Pick Universal Data Model (Pick UDM), which we created, and are capable of handling data from many sources. The Pick UDM is a core component across the MDMS, XDMS and PDP product lines.

The MDMS product line consists principally of the D3 Data Base Management System (D3), which operates on many systems including but not limited to IBM AIX, Linux and Windows NT. D3 allows application programmers to create new business solution software in less time than it normally takes in many other environments. This can translate into lower costs for the developer, lower software prices for the customer and reduced costs of ownership for both the developer and end user. Our MDMS products also include mvEnterprise, a scalable multidimensional database solution that allows the user to leverage the capabilities of the UNIX operating system, and mvBase, a multidimensional database solution that runs on all Windows platforms.

Our first XDMS product, TigerLogic version 1.1, was released in May 2003. TigerLogic XDMS is a high-performance information infrastructure software that provides both scalability, XA-compliant transactional integrity and fine-grain search capabilities typically associated with enterprise databases, as well as the dynamic extensibility, n-tier hierarchies and ease of use and deployment, mostly found in data repositories and file systems. We have filed a patent application related to the technology utilized in the TigerLogic product and this patent was pending as of June 30, 2004.

In September 2003, we announced the production release of the Pick Data Provider for .NET. The PDP component for the Microsoft .NET Framework is tightly integrated with Microsoft Visual Studio .NET. It allows software developers using IBM s Universe and Unidata databases and our D3 database platform to build Client/Server applications, Web applications or Web services using any of the languages and technologies that run on the Microsoft ..NET Framework, such as Microsoft ASP.NET, Visual Basic .NET, Visual C# .NET and Visual J# .NET.

Our RAD products support the full life cycle of software application development and are designed for rapid prototyping, development and deployment of graphical user interface (GUI) client/server and web applications. The RAD products include Omnis Studio, Omnis Studio for SAP and Omnis Classic and are object-oriented and component-based, providing the ability to deploy applications on operating system platforms such as Windows, Unix and Linux, as well as database environments such as MySQL, Oracle, DB2, Sybase, Microsoft SQL Server and other Open Data Base Connectivity (ODBC) compatible database management systems.

We have devoted significant resources to the research and development of our products and technology. We believe that our future success will depend largely on a strong development effort with respect to both our existing and new products. These development efforts have resulted in updates and upgrades to existing MDMS and RAD products and the launch of new products including the XDMS and PDP product lines. New product releases in all of our product lines are currently in progress. We expect to continue our research and development efforts in all product lines for the foreseeable future. We intend for these efforts to improve our operating results and increase cash flow. However, such efforts may not result in additional new products or revenue, and we can make no assurances that the recently announced products or future products will be successful.

In the United States, we sell our products through established distribution channels consisting of system integrators, specialized vertical application software developers and consulting organizations. We also sell our products directly through our sales personnel to end user organizations. Outside the United States, we maintain direct sales offices in the United Kingdom, France and Germany. Approximately 28% of our revenue came from sales through our offices located outside the United States for each of the three-month periods ended June 30, 2004 and 2003.

We sell our products in U.S. Dollars in North America, British Pounds Sterling in the United Kingdom and Euros in Germany and France. Because we recognize revenue and expense in these various currencies but report our financial results in U.S. Dollars, changes in exchange rates may cause variances in our period-to-period revenue and results of operations in future periods. Recorded foreign exchange gains and losses have not been material to our performance to date.

We license our software on a per-server basis or per-user basis. Therefore, the addition of servers or users to existing systems increases our revenue from our installed base of licenses.

Our customers may be classified into two general categories:

Independent Software Vendors and Software Developers. The majority of our revenue is derived from independent software vendors, which typically write their own vertical application software that they sell as a complete package to end user customers. This category includes value added resellers (VARs) and software-consulting companies that provide contract programming services to their customers.

Corporate Information Technology (IT) Departments.

For the three month periods ended June 30, 2004 and 2003, no single customer accounted for more than 10% of our revenue.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The discussion and analysis of our financial condition and results of operations is based on our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses and disclosure of contingent liabilities.

On an on-going basis, we evaluate our estimates, including those related to revenue recognition and accounting for intangible assets and goodwill. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

We have identified the accounting policies below as the policies critical to our business operations and the understanding of our results of operations. We believe the following critical accounting policies and the related judgments and estimates affect the preparation of our condensed consolidated financial statements:

REVENUE RECOGNITION. We recognize revenue using the residual method pursuant to the requirements of Statement of Position No. 97-2, Software Revenue Recognition (SOP 97-2), as amended. Under the residual method, revenue is recognized in a multiple element arrangement when company-specific objective evidence of fair value exists for all of the undelivered elements in the arrangement, but does not exist for one or more of the delivered elements in the arrangement. At the outset of the arrangement with the customer, we defer revenue for the fair value of our undelivered elements (e.g., contract revenue amount for maintenance) based on company-specific objective evidence of the amount such items are sold individually to our customers and recognize revenue for the remainder of the arrangement fee attributable to the elements initially delivered in the arrangement (e.g., software license) when the basic criteria in SOP 97-2 have been met.

Under SOP 97-2, revenue attributable to an element in a customer arrangement is recognized when persuasive evidence of an arrangement exists and delivery has occurred, provided the fee is fixed or determinable, collectibility is probable and the arrangement does not require significant customization of the software. If at the outset of the customer arrangement, we determine that the arrangement fee is not fixed or determinable, we defer the revenue and recognize the revenue when the arrangement fee becomes due and payable.

Professional services, maintenance and other revenue relate primarily to consulting services, maintenance and training. Maintenance revenue is initially deferred and then recognized ratably over the term of the maintenance contract, typically 12 months. Consulting and training revenue is recognized as the services are performed and is usually calculated on a time and materials basis. Such services primarily consist of implementation services related to the installation of our products and do not include significant customization to or development of the underlying software code. We do not have price protection programs, conditional acceptance agreements or warranty programs, and sales of our products are made without right of return.

INTANGIBLE ASSETS AND GOODWILL. We assess the impairment of identifiable intangibles, long-lived assets and goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We also assess the value of goodwill at least annually. Factors we consider to be important which could trigger an impairment review include the following:

Significant underperformance relative to expected historical or projected future operating results;

Timing of our revenue, significant changes in the manner of use of the acquired assets or the strategy for the overall business;

Significant negative industry or economic trends;

Significant decline in our stock price for a sustained period; and

Our market capitalization relative to net book value.

When we determine that the carrying value of intangibles and other long-lived assets may not be recoverable based upon the existence of one or more of the above indicators of impairment and the carrying value of the asset cannot be recovered from projected undiscounted cash flows, we measure any impairment based on a projected discounted cash flow method using a discount rate determined by our management to be commensurate with the risk inherent in the current business model. Significant management judgment is required in determining whether an indicator of impairment exists and in projecting cash flows.

Following the adoption of SFAS No. 142, Goodwill and Other Intangible Assets, we revised our policy for assessing and determining impairment of goodwill. The SFAS No. 142 goodwill impairment model is a two-step process. The first step is used to identify potential impairment by comparing the fair value of a reporting unit with its net book value (or carrying amount), including goodwill. If the fair value exceeds the carrying amount, goodwill of the reporting unit is considered not impaired and the second step of the impairment test is unnecessary. If the carrying amount of a reporting unit exceeds its fair value, the second step of the goodwill impairment test is performed to measure the amount of impairment loss, if any. The second step of the goodwill impairment test compares the implied fair value of the reporting unit s goodwill with the carrying amount of that goodwill. If the carrying amount of the reporting unit s goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. The implied fair value of goodwill is determined in the same manner as the amount of goodwill recognized in a business combination. That is, the fair value of the reporting unit is allocated to all of the assets and liabilities of that unit (including any unrecognized intangible assets) as if the reporting unit had been acquired in a business combination and the fair value of the reporting unit was the purchase price paid to acquire the reporting unit.

Determining the fair value of a reporting unit under the first step of the goodwill impairment test and determining the fair value of individual assets and liabilities of a reporting unit (including unrecognized intangible assets) under the second step of the goodwill impairment test is judgmental in nature and often involves the use of significant estimates and assumptions. These estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and the magnitude of any such charge. Estimates of fair value are primarily determined using discounted cash flows and are based on our best estimate of future revenue and operating costs and general market conditions. This approach uses significant assumptions, including projected future cash flows (including timing), the discount rate reflecting the risk inherent in future cash flows, and a terminal growth rate. These estimates are subject to review and approval by management. Changes to these estimates in future periods may have a material impact on the Company s financial position and results of operations.

Results of Operations

The following table sets forth certain Condensed Consolidated Statement of Operations data in total dollars, as a percentage of total net revenues and as a percentage change from the prior year. Cost of license revenues, cost of service revenues, gross profit and margin on license revenues and gross profit and margin on service revenues are expressed as a percentage of the related revenues. This information should be read in conjunction with the Condensed Consolidated Financial Statements included elsewhere in this Form 10-QSB.

	Three Months Ended June 30, 2004			Three Months Ended June 30, 2003	
	Results	**% of Net Revenues**	**Percent Change**	**Results**	**% of Net Revenues**
Net revenues					
Licenses	$ 2,222	43%	(3)%	$ 2,286	42%
Services	2,975	57%	(5)%	3,123	58%
Total net revenues	5,197	100%	(4)%	5,409	100%
Cost of revenues					
Cost of license revenues (as a % of license revenues)	72	3%	(19)%	89	4%
Cost of service revenues (as a % of service revenues)	468	16%	(4)%	489	16%
Gross profit and margin on license revenues	2,150	97%	(2)%	2,197	96%
Gross profit and margin on service revenues	2,507	84%	(5)%	2,634	84%
Operating expenses					
Selling and marketing	1,414	27%	(3)%	1,457	27%
Research and development	1,738	33%	(12)%	1,974	36%
General and administrative	889	17%	(3)%	920	17%
Stock-based compensation	32	1%	(36)%	50	1%
Amortization of goodwill and intangible assets	650	13%	0%	650	12%
Total operating expenses	4,723	91%	(6)%	5,051	93%
Operating loss	(66)	(1)%	(70)%	(220)	(4)%
Other income (expense), net	(313)	(6)%	12%	(280	