

Limelight Networks, Inc.  
Form 10-Q  
November 05, 2010  
Table of Contents

**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 September 30, 2010

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-33508

**LIMELIGHT NETWORKS, INC.**

*(Exact name of registrant as specified in its charter)*

**Delaware**  
*(State or other jurisdiction of  
incorporation or organization)*

**20-1677033**  
*(I.R.S. Employer*

*Identification No.)*

**2220 W. 14<sup>th</sup> Street**

**Tempe, AZ 85281**

*(Address of principal executive offices, including Zip Code)*

**(602) 850-5000**

*(Registrant's telephone number, including area code)*

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

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

Large accelerated filer

Accelerated filer

Non-accelerated filer   
(Do not check if a smaller

Smaller reporting company

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

The number of shares outstanding of the registrant's common stock as of November 2, 2010: 99,117,655 shares.

**Table of Contents**

**LIMELIGHT NETWORKS, INC.**

**FORM 10-Q**

**Quarterly Period Ended September 30, 2010**

**TABLE OF CONTENTS**

	<b>Page</b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	<b>3</b>
ITEM 1. <b><u>FINANCIAL STATEMENTS</u></b>	<b>3</b>
<u>Condensed Consolidated Balance Sheets as of September 30, 2010 and December 31, 2009</u>	3
<u>Condensed Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2010 and 2009</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2010 and 2009</u>	5
<u>Notes to Unaudited Condensed Consolidated Financial Statements for the Three and Nine Months Ended September 30, 2010 and 2009</u>	6
ITEM 2. <b><u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u></b>	<b>23</b>
ITEM 3. <b><u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u></b>	<b>37</b>
ITEM 4. <b><u>CONTROLS AND PROCEDURES</u></b>	<b>37</b>
<b><u>PART II. OTHER INFORMATION</u></b>	<b>38</b>
ITEM 1. <b><u>LEGAL PROCEEDINGS</u></b>	<b>38</b>
ITEM 1A. <b><u>RISK FACTORS</u></b>	<b>39</b>
ITEM 2. <b><u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u></b>	<b>54</b>
ITEM 3. <b><u>DEFAULTS UPON SENIOR SECURITIES</u></b>	<b>55</b>
ITEM 4. <b><u>REMOVED AND RESERVED</u></b>	<b>55</b>
ITEM 5. <b><u>OTHER INFORMATION</u></b>	<b>55</b>
ITEM 6. <b><u>EXHIBITS</u></b>	<b>56</b>
<b><u>SIGNATURES</u></b>	<b>57</b>
EX-10.32	
EX-31.01	
EX-31.02	
EX-32.01	
EX-32.02	

**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****LIMELIGHT NETWORKS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except per share data)**

	<b>September 30, 2010 (Unaudited)</b>	<b>December 31, 2009</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 52,229	\$ 89,509
Marketable securities	18,421	64,870
Accounts receivable, net of reserves of \$7,491 at September 30, 2010 and \$9,226 at December 31, 2009	39,085	26,363
Income taxes receivable	862	617
Prepaid expenses and other current assets	8,891	9,654
Total current assets	119,488	191,013
Property and equipment, net	51,785	35,524
Marketable securities, less current portion	2,024	12
Goodwill	97,975	619
Other intangible assets, net	19,912	370
Other assets	7,520	8,132
Total assets	\$ 298,704	\$ 235,670
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 10,909	\$ 5,144
Deferred revenue, current portion	10,049	12,199
Capital lease obligation, current portion	970	
Other current liabilities	19,464	14,140
Total current liabilities	41,392	31,483
Deferred revenue, less current portion		1,377
Capital lease obligation, less current portion	1,706	
Deferred income tax, less current portion	602	10
Other long term liabilities	21	
Total liabilities	43,721	32,870
Commitments and contingencies		
Stockholders' equity:		
Convertible preferred stock, \$0.001 par value; 7,500 shares authorized; 0 shares issued and outstanding		
Common stock, \$0.001 par value; 150,000 shares authorized at September 30, 2010; 98,995 and 85,011 shares issued and outstanding at September 30, 2010 and December 31, 2009, respectively	99	85
Additional paid-in capital	374,053	308,537

Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Accumulated other comprehensive income	750	93
Accumulated deficit	(119,919)	(105,915)
Total stockholders' equity	254,983	202,800
Total liabilities and stockholders' equity	\$ 298,704	\$ 235,670

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

**Table of Contents****LIMELIGHT NETWORKS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except per share data)****(Unaudited)**

	<b>For the Three Months Ended September 30,</b>		<b>For the Nine Months Ended September 30,</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
Revenues	\$ 49,803	\$ 32,530	\$ 128,084	\$ 98,038
Cost of revenue:				
Cost of services	22,068	14,889	56,773	44,757
Depreciation network	5,878	6,018	15,980	18,699
Total cost of revenue	27,946	20,907	72,753	63,456
Gross margin	21,857	11,623	55,331	34,582
Operating expenses:				
General and administrative	8,359	6,405	26,095	24,714
Sales and marketing	12,724	8,060	33,429	23,915
Research and development	4,491	2,024	10,614	5,878
Depreciation and amortization	2,034	627	4,404	1,699
Provision for litigation judgment				(65,645)
Total operating expenses	27,608	17,116	74,542	(9,439)
Operating (loss) income	(5,751)	(5,493)	(19,211)	44,021
Other income (expense):				
Interest expense	(6)	(11)	(13)	(33)
Interest income	210	330	767	1,050
Other (expense) income	(120)	15	(117)	131
Total other income, net	84	334	637	1,148
(Loss) income before income taxes	(5,667)	(5,159)	(18,574)	45,169
Income tax expense (benefit)	287	61	(4,570)	552
Net (loss) income	\$ (5,954)	\$ (5,220)	\$ (14,004)	\$ 44,617
Net (loss) income per weighted average share:				
Basic	\$ (0.06)	\$ (0.06)	\$ (0.15)	\$ 0.53
Diluted	\$ (0.06)	\$ (0.06)	\$ (0.15)	\$ 0.51
Shares used in per weighted average share calculations:				
Basic	98,634	84,489	92,547	84,012

Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Diluted

98,634

84,489

92,547

87,708

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

**Table of Contents****LIMELIGHT NETWORKS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)**

	<b>For the Nine Months Ended September 30, 2010      2009 (Unaudited)</b>	
<b>Cash flows from operating activities:</b>		
Net (loss) income	\$ (14,004)	\$ 44,617
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	20,384	20,398
Share-based compensation	13,058	13,137
Deferred income taxes	(190)	
Income tax benefit related to business acquisition	(5,768)	
Provision for litigation		(65,645)
Accounts receivable charges	2,342	4,239
Loss (gain) on foreign currency transactions	(5)	181
Loss on sale of property and equipment	152	
Accretion of marketable securities	274	(455)
Loss on marketable securities		
Changes in operating assets and liabilities:		
Accounts receivable	(5,506)	1,793
Prepaid expenses and other current assets	1,138	(1,347)
Income taxes receivable	158	(176)
Other assets	1,006	(8,314)
Accounts payable	(1,033)	(5,198)
Deferred revenue	(4,290)	(2,085)
Other current liabilities	(134)	(6,704)
Other long term liabilities	21	
Net cash provided by (used in) operating activities	7,603	(5,559)
<b>Cash flows from investing activities:</b>		
Purchase of marketable securities	(27,470)	(45,735)
Sale of marketable securities	73,585	32,400
Purchases of property and equipment	(25,405)	(16,648)
Acquisition of businesses, net of cash acquired	(66,529)	22
Net cash used in investing activities	(45,819)	(29,961)
<b>Cash flows from financing activities:</b>		
Proceeds from exercise of stock options	462	240
Net cash provided by financing activities	462	240
Effect of exchange rate changes on cash	474	(453)
Net decrease in cash and cash equivalents	(37,280)	(35,733)



Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Cash and cash equivalents at beginning of period	89,509	138,180
Cash and cash equivalents at end of period	\$ 52,229	\$ 102,447
<b>Supplemental disclosure of cash flow information:</b>		
Cash paid for interest	\$ 13	\$
Cash paid for income taxes	\$ 1,499	\$ 751
Property and equipment purchases remaining in accounts payable and other current liabilities	\$ 5,157	\$ 3,373
Assets acquired thru capital leases	\$ 2,676	\$
Common stock issued in connection with acquisition of businesses	\$ 52,642	\$ 962

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

---

**Table of Contents**

**LIMELIGHT NETWORKS, INC.**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. Nature of Business**

Limelight Networks, Inc. (the Company) provides on-demand software, platform, and infrastructure services that help global businesses reach and engage audiences online or on any mobile or connected device, enabling them to enhance their brand presence, build stronger customer relationships, analyze viewer preferences, optimize their advertising, and manage and monetize their digital assets. The Company services customers in North America, Europe, Middle East and Africa (EMEA) and the Asia Pacific region.

**2. Summary of Significant Accounting Policies and Use of Estimates**

***Basis of Presentation***

The condensed consolidated financial statements include accounts of the Company and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated. The accompanying condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (GAAP) and pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). These principles require management to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, together with amounts disclosed in the related notes to the condensed consolidated financial statements. Actual results and outcomes may differ from management's estimates, judgments and assumptions. Significant estimates used in these condensed consolidated financial statements include, but are not limited to, revenues, accounts receivable and related reserves, useful lives and realizability of long-term assets, capitalized software, acquired intangibles, provision for litigation, income and other taxes, the fair value of stock-based compensation and other contingent liabilities. Estimates are periodically reviewed in light of changes in circumstances, facts and experience. The effects of material revisions in estimates are reflected in the condensed consolidated financial statements prospectively from the date of the change in estimate. The accompanying condensed consolidated balance sheet as of September 30, 2010, the condensed consolidated statements of operations for the three and nine months ended September 30, 2010 and 2009, and the condensed consolidated statements of cash flows for the nine months ended September 30, 2010 and 2009, are unaudited. The condensed consolidated balance sheet information as of December 31, 2009 is derived from the audited consolidated financial statements which were included in our Annual Report on Form 10-K filed with the SEC on March 12, 2010. The consolidated financial information contained in this Quarterly Report on Form 10-Q should be read in conjunction with the audited consolidated financial statements and related notes contained in the Annual Report on Form 10-K filed on March 12, 2010.

The results of operations presented in this Quarterly Report on Form 10-Q are not necessarily indicative of the results that may be expected for the year ending December 31, 2010 or for any future periods. In the opinion of management, these unaudited condensed consolidated financial statements include all adjustments of a normal recurring nature that are necessary to present fairly the results of all interim periods reported herein.

***Revenue Recognition***

The Company derives revenue from the sale of services to customers executing contracts having terms of one year or longer. These contracts generally commit the customer to a minimum monthly or annual level of usage and provide the rate at which the customer must pay for actual usage above the monthly or annual minimum. For these services, the Company recognizes the monthly minimum as revenue each month provided that an enforceable contract has been signed by both parties, the service has been delivered to the customer, the fee for the service is fixed or determinable and collection is reasonably assured. Should a customer's usage of the Company's services exceed the monthly minimum commitment, the Company recognizes revenue for such excess in the period of the usage. For annual or other non-monthly period revenue commitments, the Company recognizes revenue monthly based upon the customer's actual usage each month of the commitment period and only recognizes any remaining committed amount for the applicable period in the last month thereof. The Company typically charges the customer an installation fee when the services are first activated. The installation fees are recorded as deferred revenue and recognized as revenue ratably over the estimated life of the customer arrangement. The Company also derives revenue from campaigns, services and events sold as discrete, non-recurring events or based solely on usage. For these services, the Company recognizes revenue after an enforceable contract has been signed by both parties, the fee is fixed or determinable, the event or usage has occurred and collection is reasonably assured.

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

The Company has on occasion entered into multi-element arrangements. In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2009-13, Revenue Recognition (Topic 605) Multiple-Deliverable Revenue Arrangements. ASU 2009-13 addresses the accounting for multiple-deliverable arrangements to enable vendors to account for products or services (deliverables) separately rather than as a combined unit. Specifically, this guidance amends the criteria in Subtopic 605-25, Revenue Recognition-Multiple-Element Arrangements (Subtopic 605-25), for separating consideration in multiple-deliverable arrangements. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence; (b) third-party evidence; or (c) management's best estimate. This guidance also eliminates the residual method of allocation and requires that arrangement consideration be allocated at the inception of the

---

**Table of Contents**

arrangement to all deliverables using the relative selling price method. In the third quarter of 2010, the Company early adopted ASU 2009-13 with such adoption being effective for revenue arrangements entered into or materially modified after January 1, 2010. The Company did not enter into or modify any multi-element arrangements falling under the scope of ASU 2009-13 during the six months ended June 30, 2010. The Company recognized \$1.1 million of revenue related to a multi-element arrangement accounted for in accordance with ASU 2009-13 during the three and nine month periods ended September 30, 2010. In October 2009, the FASB also issued ASU 2009-14, Software (Topic 985) Certain Revenue Arrangements That Include Software Elements. ASU 2009-14 changes revenue recognition for tangible products containing software and hardware elements. Specifically, tangible products containing software and hardware that function together to deliver the tangible products essential functionality are scoped out of the existing software revenue recognition guidance and will be accounted for under the multiple-element arrangements revenue recognition guidance under ASU 2009-13. In the third quarter of 2010 in conjunction with the adoption of ASU 2009-13, the Company early adopted ASU 2009-14 with such adoption being effective for revenue arrangement entered into or materially modified after January 1, 2010. The Company did not enter into or modify any arrangements falling under the scope of ASU 2009-14 during the nine months ended September 30, 2010, and accordingly the impact of adoption was not material to the Company's financial position, results of operations or cash flows.

Prior to the adoption of ASU 2009-13 effective January 1 2010, the Company accounted for multiple element arrangements in accordance with Subtopic 605-25. When the Company entered into such arrangements, each element was accounted for separately over its respective service period or at the time of delivery, provided that there was objective evidence of fair value for the separate elements. Objective evidence of fair value includes the price charged for the element when sold separately. If the fair value of each element could not be objectively determined, the total value of the arrangement was recognized ratably over the entire service period to the extent that all services have begun to be provided, and other revenue recognition criteria have been satisfied.

If the multi-element arrangement included a significant software component, the Company recognized software license revenue when persuasive evidence of an arrangement exists, delivery occurs, the fee is fixed or determinable and collection of the receivable is reasonably assured. If a software license contained an undelivered element, the vendor-specific objective evidence (VSOE) of fair value of the undelivered element is deferred and the revenue recognized once the element is delivered. The undelivered elements related to these arrangements are primarily software support and professional services. VSOE of fair value of software support and professional services is based upon hourly rates or fixed fees charged when those services are sold separately. If VSOE could not be established for all elements to be delivered, the Company deferred all amounts received under the arrangement and did not begin to recognize revenue until the delivery of the last element of the contract started. Subsequent to commencement of delivery of the last element, the Company commenced revenue recognition. Amounts to be received under the contract are then included in the amortizable base and recognized as revenue ratably over the remaining term of the arrangement until the Company has delivered all elements and has no additional performance obligations.

The Company has certain multi-element arrangements as of September 30, 2010 that were entered into prior to the adoption of ASU 2009-13 in 2010. Under these arrangements, the Company recognized approximately \$3.9 million and \$9.2 million, respectively, in revenue for the three and nine month periods ended September 30, 2010. During the three and nine month periods ended September 30, 2009, the Company recognized approximately \$1.8 million and \$5.1 million, respectively, in revenue related to its multi-element arrangement. As of September 30, 2010, the Company had deferred revenue related to these multi-element arrangements of approximately \$4.3 million that will be recognized over the remaining terms of the respective arrangements based on the underlying elements of the arrangements in accordance with the Company's revenue recognition policies.

The Company also sells services through a reseller channel. Assuming all other revenue recognition criteria are met, revenue from reseller arrangements is recognized over the term of the contract, based on the reseller's contracted non-refundable minimum purchase commitments plus amounts sold by the reseller to its customers in excess of the minimum commitments. These excess commitments are recognized as revenue in the period in which the service is provided. The Company records revenue under these agreements on a net or gross basis depending upon the terms of the arrangement. The Company typically records revenue gross when it has risk of loss, latitude in establishing price, credit risk and is the primary obligor in the arrangement. Reseller revenue for the three and nine month periods ended September 30, 2010 represented approximately 5% respectively, of the Company's total revenue. During the three and nine month periods ended September 30, 2009, reseller revenue was approximately 3% and 2%, respectively, of the Company's total revenue.

From time to time, the Company enters into contracts to sell services to unrelated companies at or about the same time the Company enters into contracts to purchase products or services from the same companies. If the Company concludes that these contracts were negotiated concurrently, the Company records as revenue only the net cash received from the vendor. For certain non-cash arrangements whereby the Company provides rack space and bandwidth services to several companies in exchange for advertising the Company records barter revenue and expense if the services are objectively measurable. The various types of advertising include radio, website, print and signage. The Company recorded barter revenue and expense of approximately \$22,000 and \$74,000, respectively, for the three and nine month periods ended September 30, 2010. During the three and nine month periods ended September 30, 2009, the Company recorded barter revenue and expense of approximately \$0- and \$172,000, respectively.



**Table of Contents**

The Company may from time to time resell licenses or services of third parties. Revenue for these transactions is recorded when the Company has risk of loss related to the amounts purchased from the third party and the Company adds value to the license or service, such as by providing maintenance or support for such license or service. If these conditions are present, the Company recognizes revenue when all other revenue recognition criteria are satisfied.

At the inception of a customer contract for service, the Company makes an assessment as to that customer's ability to pay for the services provided. If the Company subsequently determines that collection from the customer is not reasonably assured, the Company records an allowance for doubtful accounts and bad debt expense or deferred revenue for all of that customer's unpaid invoices and ceases recognizing revenue for continued services provided until cash is received.

**Restricted Cash**

The Company secures one of its capital lease obligations with a letter of credit that is collateralized by \$263,000 of cash. When the capital lease is repaid, the letter of credit would no longer be required and the restricted cash would be available for general use. In addition, the Company secures a business credit card with a letter of credit that is collateralized by approximately \$50,000 of cash. Restricted cash is excluded from cash and cash equivalents and is recorded in other long term assets (due to the term of the lease being greater than one year and the expectation that the usage of the credit card will continue beyond one year) in the accompanying balance sheets.

**Investments in Marketable Securities**

Management determines the appropriate classification of its debt and equity securities at the time of purchase and reevaluates such classification as of each balance sheet date. Realized gains and losses and declines in value judged to be other than temporary are determined based on the specific identification method and are reported in the statements of operations.

The Company has classified its investments in equity and debt securities as available-for-sale. Available-for-sale investments are initially recorded at cost with temporary changes in fair value periodically adjusted through comprehensive income. The Company periodically reviews its investments for other-than-temporary declines in fair value based on the specific identification method and writes down investments to their fair value when an other-than-temporary decline has occurred.

The following is a summary of available-for-sale securities at September 30, 2010 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Government agency bonds	\$ 11,336	\$ 5	\$ (1)	\$ 11,340
Corporate notes and bonds	7,056	25		7,081
Total available-for-sale debt securities	18,392	30	(1)	18,421
Publicly traded common stock	1,279	745		2,024
Total available-for-sale securities	\$ 19,671	\$ 775	\$ (1)	\$ 20,445

At September 30, 2010, the Company evaluated its investment portfolio in available-for-sale debt securities, and noted unrealized losses of approximately \$1,000 were due to fluctuations in interest rates. Management does not believe any of the unrealized losses represented an other-than-temporary impairment based on its evaluation of available evidence as of September 30, 2010. There have been no unrealized losses greater than twelve months. The Company's intent is to hold these investments until such time as these assets are no longer impaired.

Expected maturities can differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties, and the Company views its available-for-sale securities as available for current operations.

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

The amortized cost and estimated fair value of the available-for-sale debt securities at September 30, 2010, by maturity, are shown below (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale debt securities				
Due in one year or less	\$ 16,392	\$ 29	\$ (1)	\$ 16,420
Due after one year and through five years	2,000	1		2,001
	\$ 18,392	\$ 30	\$ (1)	\$ 18,421

**Table of Contents**

The following is a summary of available-for-sale securities at December 31, 2009 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Government agency bonds	\$ 46,153	\$ 16	\$ (33)	\$ 46,136
Commercial paper	8,996			8,996
Corporate notes and bonds	9,631	108	(1)	9,738
Total available-for-sale debt securities	64,780	124	(34)	64,870
Publicly traded common stock	13		(1)	12
Total available-for-sale securities	\$ 64,793	\$ 124	\$ (35)	\$ 64,882

The amortized cost and estimated fair value of the available-for-sale debt securities at December 31, 2009, by maturity, are shown below (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale debt securities				
Due in one year or less	\$ 62,223	\$ 124	\$ (27)	\$ 62,320
Due after one year and less than two years	2,557		(7)	2,550
	\$ 64,780	\$ 124	\$ (34)	\$ 64,870

**Goodwill and Other Intangible Assets**

Goodwill represents costs in excess of fair values assigned to the underlying net assets of the acquired company. Goodwill is not amortized but instead is tested for impairment annually or more frequently if events or changes in circumstances indicate the asset might be impaired.

The Company's other intangible assets represent existing technologies, trademark, non-compete agreements, patent, usage contract, domain names and customer relationships intangibles. Other intangible assets are amortized over their respective estimated lives, ranging from one to five years. In the event that facts and circumstances indicate intangibles or other long-lived assets may be impaired, the Company evaluates the recoverability and estimated useful lives of such assets.

**Recently Issued Accounting Pronouncements**

In February 2010, the FASB issued FASB Accounting Standards Update 2010-09, *Subsequent Events: Amendments to Certain Recognition and Disclosure Requirements* (ASU 2010-09), which amends FASB ASC Topic 855, *Subsequent Events*. The update provides that SEC filers, as defined in ASU 2010-09, are no longer required to disclose the date through which subsequent events have been evaluated in originally issued and revised financial statements. The update also requires SEC filers to evaluate subsequent events through the date the financial statements are issued rather than the date the financial statements are available to be issued. The Company adopted ASU 2010-09 upon issuance. This update had no impact on the Company's financial position, results of operations or cash flows.

As of January 1, 2010, the Company adopted Accounting Standards Update 2010-06 *Fair Value Measurements and Disclosures* (Topic 820) *Improving Disclosures about Fair Value Measurements*. This new accounting standard requires new disclosures and clarifies certain existing disclosure requirements about fair value measurements. The standard requires a reporting entity to disclose significant transfers in and out of Level 1 and Level 2 fair value measurements, to describe the reasons for the transfers and to present separately information about



## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

purchases, sales, issuances and settlements for fair value measurements using significant unobservable inputs. The standard is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements, which is effective for interim and annual reporting periods beginning after December 15, 2010; early adoption is permitted. The adoption of the standard did not have a material impact on the Company's financial position, results of operations or cash flows.

As of January 1, 2010, the Company adopted Accounting Standards Update 2010-02, *Consolidation (Topic 810) Accounting and Reporting for Decreases in Ownership of a Subsidiary*. This new accounting standard clarifies the scope of the decrease in ownership provisions and expands the disclosure requirements about deconsolidation of a subsidiary or de-recognition of a group of assets. The standard is effective beginning in the first interim or annual reporting period ending on or after December 15, 2009 and thus is effective for the Company's first quarter reporting in 2010. The amendments in the standard must be applied retrospectively to the first period that an entity adopted SFAS 160. The adoption of the standard did not have a material impact on the Company's financial position, results of operations or cash flows.

**Table of Contents****3. Business Acquisitions***chors GmbH*

On January 27, 2010 the Company acquired chors GmbH (chors), an on-line and direct marketing solutions provider located in Germany. The aggregate purchase price, including the earn-out provision, consisted of approximately \$2.8 million of cash, of which approximately \$2.5 million was paid at closing, and up to 860,000 shares of the Company's common stock, of which 86,000 shares were issued at closing. The fair value of the common shares issued as consideration for chors was determined on the basis of the closing market price of the Company's common shares on the acquisition date. In addition, the Company incurred approximately \$0.3 million of transaction costs, which primarily consisted of fees for legal and financial advisory services. These transaction costs were included in general and administrative expenses in the Company's statement of operations for the three (approximately \$0.1 million) and nine (approximately \$0.3 million) month periods ended September 30, 2010. The Company's consolidated financial statements include the results of operations of chors from the date of acquisition. The historical results of operations of chors were not significant to the Company's consolidated results of operations for the periods presented. The total purchase consideration was allocated to the assets acquired and liabilities assumed at their estimated fair values as of the date of acquisition, as determined by management and, with respect to identifiable intangible assets, by management with the assistance of an appraisal provided by a third party valuation firm. The excess of the purchase price over the amounts allocated to assets acquired and liabilities assumed has been recorded as goodwill. In accordance with current accounting standards, goodwill associated with the chors acquisition will not be amortized and will be tested for impairment at least annually (see Note 6). As of September 30, 2010, the Company has recorded approximately \$3.1 million of contingent consideration based on current estimates to achieve the financial milestones in the earn-out provision.

The following table presents the allocation of the purchase price for chors:

	<b>(In thousands)</b>
<b>Consideration:</b>	
Cash	\$ 2,814
Value of common stock	3,122
 Total consideration	 \$ 5,936
<b>Acquisition-related costs (included in general and administrative expenses)</b>	<b>\$ 265</b>
 <b>Recognized amounts of identifiable assets acquired and liabilities assumed:</b>	
Financial assets	\$ 845
Property and equipment	63
Identifiable intangible assets	2,498
Financial liabilities	(557)
 Total identifiable net assets	 2,849
Goodwill	3,087
	 \$ 5,936

The following were the identified intangible assets acquired and the respective estimated periods over which such assets will be amortized:

	<b>Amount</b>	<b>Weighted</b>
	<b>(In thousands)</b>	<b>Average</b>
		<b>useful life</b>
		<b>(In years)</b>
Existing technologies	\$ 1,180	3.0

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Non-compete agreements	940	4.0
Usage contract	370	1.6
Trademarks	8	5.0
<b>Total</b>	<b>\$ 2,498</b>	

In determining the purchase price allocation, the Company considered, among other factors, its intention to use the acquired assets and the historical and estimated future demand for chors services. The fair value of intangible assets was based upon the market approach and the income approach. In applying the market approach, the values of the intangible assets acquired were determined based upon the economic principal of competition. Although there is no established public market for intangible assets, the market approach can be utilized through the analysis of market-derived empirical transaction data. The market approach involves empirical market data involving comparable intangible assets and a comparison of the subject intangible assets to such comparable intangible assets. This method is sometimes referred to as the Net Avoided Royalty Method. In the Net Avoided Royalty Method, transactions

**Table of Contents**

involving the licensing of comparable intangible assets are analyzed and the value of an asset is estimated by capitalizing the royalty expense saved because the company owns the asset.

The relief-from-royalty method was used to value the existing technologies and trademarks acquired from chors. The relief-from-royalty method estimates the cost savings that accrue to the owner of an intangible asset that would otherwise be required to pay royalties or license fees on revenues earned through the use of the asset. The royalty rate used is based on an analysis of empirical, market-derived royalty rates for guideline intangible assets. Typically, revenue is projected over the expected remaining useful life of the completed technology. The market-derived royalty rate is then applied to estimate the royalty savings. The key assumptions used in valuing the existing technologies are as follows: royalty rate of 14%, discount rate of 21.5%, tax rate of 25% and estimated average economic life of three years. The key assumptions used in valuing the existing trademarks are as follows: royalty rate of 0.5%, discount rate of 21%, tax rate of 25% and estimated average economic life of five years.

The non-compete agreements and usage contract were valued using the income approach. In utilizing the income approach, the Company estimates the value of an intangible based on the present value of future economic income attributable to the ownership of the asset. This approach is typically determined through a Discounted Cash Flow Method. The Discounted Cash Flow Method provides an indication of value based on discounting projected debt-free net cash flows to their present value at a discount rate that reflects both market based return requirements and risks inherent in the specific intangible asset. In applying this approach, the values of the intangible assets acquired were determined using projections of revenues and expenses specifically attributed to the intangible assets. The income streams were then discounted to present value using estimated risk-adjusted discount rates. The rate used to discount the expected future net cash flows from the intangible assets to their present values was based upon a weighted average cost of capital of approximately 20%. The discount rate was determined after consideration of market rates of return on debt and equity capital, the weighted average return on invested capital and the risk associated with achieving forecasted sales related to the technology and assets acquired from chors. The key assumptions used in valuing the non-compete agreements and usage contract were as follows: 20.5% for non-compete agreements, and 18.5% for usage contract, tax rate of 25% and estimated remaining economic life of 4 years for non-compete agreements and 1.6 years for the usage contract.

The total weighted average amortization period for the intangible assets acquired from chors is 3.2 years. The intangible assets are being amortized based upon the pattern in which the economic benefits of the intangible assets are being utilized, which in general reflects the cash flows generated from such assets. The goodwill resulting from the chors acquisition is not deductible for income tax purposes.

***EyeWonder Acquisition***

On April 30, 2010, the Company completed its acquisition of EyeWonder, Inc. (EyeWonder), a provider of interactive digital advertising products and services to advertisers, advertising agencies and publishers headquartered in Atlanta, Georgia. The aggregate purchase price, excluding the earn-out provision consisted of approximately \$62.8 million of cash and 12,740,000 shares of the Company's common stock with an estimated fair value of approximately \$51.2 million. The fair value of the common shares issued as consideration for EyeWonder was determined on the basis of the closing market price of the Company's common shares on the acquisition date. Under the terms of the Merger Agreement, the former holders of EyeWonder securities that were outstanding immediately prior to the completion of the merger received, in the aggregate, approximately \$49.6 million in cash and 9,726,301 shares of the Company's common stock with a determined value of approximately \$39.1 million based on the closing price of the Company's common stock on April 30, 2010. In addition, the former EyeWonder securityholders may receive up to 4,774,000 shares of the Company's common stock and approximately \$0.3 million in cash in April 2011 if certain performance metrics are satisfied. At this time, the Company does not believe that the performance metrics will be achieved and accordingly has not recorded any contingent consideration. Under the terms of the Merger Agreement, 3,013,699 shares of the Company's common stock have been set aside in an escrow account and will be held until June 28, 2011, subject to any unresolved indemnification claims. In addition, the Company incurred approximately \$2.3 million of transaction costs, which primarily consisted of fees for legal and financial advisory services. Approximately \$1.5 million of these costs were recorded in 2009 and approximately \$0.8 million, are included in general and administrative expenses in the Company's statement of operations for the nine month period ended September 30, 2010. The Company's consolidated financial statements include the results of operations of EyeWonder from the date of acquisition. The total purchase consideration was allocated to the assets acquired and liabilities assumed at their estimated fair values as of the date of acquisition, as determined by management and, with respect to identifiable intangible assets, by management with the assistance of an appraisal provided by a third party valuation firm. The allocation is preliminary and will be finalized during the fourth quarter of 2010. The excess of the purchase price over the amounts allocated to assets acquired and liabilities assumed has been recorded as goodwill. The value of the goodwill from this acquisition can be attributed to a number of business factors including, but not limited to, potential sales opportunities of providing Limelight services to EyeWonder customers; trained technical workforce in place in the United States and Europe; existing sales pipeline and trained sales force and potential cost synergies to be realized. In accordance with current accounting standards, goodwill associated with the EyeWonder acquisition will not be amortized and will be tested for impairment at least annually (see Note 6).



**Table of Contents**

The following table presents the preliminary allocation of the purchase price for EyeWonder:

	(In thousands)
<b>Consideration:</b>	
Cash	\$ 62,782
Common stock	51,215
Total consideration	\$ 113,997
<b>Acquisition-related costs (included in general and administrative expenses)</b>	<b>\$ 2,331</b>
<b>Recognized amounts of identifiable assets acquired and liabilities assumed:</b>	
Financial assets	\$ 12,798
Property and equipment	1,100
Identifiable intangible assets	17,849
Financial liabilities	(8,617)
Total identifiable net assets	23,130
Goodwill	90,867
	<b>\$ 113,997</b>

The following were the preliminary identified intangible assets acquired and the respective estimated periods over which such assets will be amortized:

	Amount (In thousands)	Weighted Average useful life (In years)
Existing technologies	\$ 14,982	4.0
Patent	789	4.0
Trademarks	1,800	Indefinite
Non-compete agreements	278	1.5
Total	\$ 17,849	

In determining the purchase price allocation, the Company considered, among other factors, its intention to use the acquired assets and the historical and estimated future demand for EyeWonder services. The estimated fair value of intangible assets was based upon the market approach and the income approach. In applying the market approach, the values of the intangible assets acquired were determined based upon the economic principal of competition. Although there is no established public market for intangible assets, the market approach can be utilized through the analysis of market-derived empirical transaction data. The market approach involves empirical market data involving comparable intangible assets and a comparison of the subject intangible assets to such comparable intangible assets. This method is sometimes referred to as the Net Avoided Royalty Method. In the Net Avoided Royalty Method, transactions involving the licensing of comparable intangible assets are analyzed and the value of an asset is estimated by capitalizing the royalty expense saved because the company owns the asset.

The relief-from-royalty method was used to value the existing technologies, patents and trademarks acquired from EyeWonder. The relief-from-royalty method estimates the cost savings that accrue to the owner of an intangible asset that would otherwise be required to pay royalties or license fees on revenues earned through the use of the asset. The royalty rate used is based on an analysis of empirical, market-derived royalty rates for guideline intangible assets. Typically, revenue is projected over the expected remaining useful life of the

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

completed technology. The market-derived royalty rate is then applied to estimate the royalty savings. The key assumptions used in valuing the existing technologies and patents acquired are as follows: royalty rate of 14%, discount rate of 17%, tax rate of 38% and estimated average economic life of four years. The key assumptions used in valuing the existing trademarks acquired are as follows: royalty rate of 0.5%, discount rate of 17%, tax rate of 38% and an indefinite economic life.

The non-compete agreements were valued using the income approach. In utilizing the income approach, the Company estimates the value of an intangible based on the present value of future economic income attributable to the ownership of the asset. This approach is typically determined through a Discounted Cash Flow Method. The Discounted Cash Flow Method provides an indication of value based on discounting projected debt-free net cash flows to their present value at a discount rate that reflects both market based return requirements and risks inherent in the specific intangible asset. In applying this approach, the values of the intangible assets acquired were determined using projections of revenues and expenses specifically attributed to the intangible assets. The income streams were then discounted to present value using estimated risk-adjusted discount rates. The rate used to discount the expected future net cash flows from the intangible assets to their present values was based upon a weighted average cost of capital of approximately 16%. The discount rate was determined after consideration of market rates of return on debt and equity capital, the weighted average return on invested capital and the risk associated with achieving forecasted sales related to the technology and

**Table of Contents**

assets acquired from EyeWonder. The key assumptions used in valuing the non-compete agreements were as follows: discount rate of 16%, tax rate of 38% and estimated remaining economic life of 1.5 years.

The total weighted average amortization period for the intangible assets acquired from EyeWonder is 3.6 years. The intangible assets are being amortized based upon the pattern in which the economic benefits of the intangible assets are being utilized, which in general reflects the cash flows generated from such assets. The goodwill resulting from the EyeWonder acquisition is not deductible for income tax purposes.

The following table reflects unaudited pro forma results of operations of the Company for the three and nine months ended September 30, 2010 and 2009 assuming that the EyeWonder acquisition had occurred on January 1, 2010 and January 1, 2009, respectively (in thousands, except per share data):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenues	\$ 49,803	\$ 41,868	\$ 137,604	\$ 121,192
Net income	\$ (6,126)	\$ (5,601)	\$ (16,475)	\$ 41,145
Net income per share basic	\$ (0.06)	\$ (0.06)	\$ (0.18)	\$ 0.43
Net income per share diluted	\$ (0.06)	\$ (0.06)	\$ (0.18)	\$ 0.41

***Delve Networks, Inc. Acquisition***

On July 30, 2010, the Company acquired Delve Networks, Inc. (Delve), a privately-held provider of cloud-based video publishing and analytics services located in Seattle, Washington. The aggregate purchase price consisted of approximately \$2.6 million of cash paid at the closing and approximately \$0.2 million for the earn-out provision and 335,195 shares of the Company's common stock with an estimated fair value of approximately \$1.4 million. The fair value of the common shares issued as consideration for Delve was determined on the basis of the closing market price of the Company's common shares on the acquisition date. Under the terms of the Merger Agreement, approximately \$0.6 million of the cash portion of the purchase price has been set aside in an escrow account and will be held for a period of up to 36 months following the closing date to satisfy any unresolved indemnification claims. In addition, the Company incurred approximately \$0.2 million of transaction costs, which primarily consisted of fees for legal services. These transaction costs were included in general and administrative expenses in the Company's statement of operations for the three and nine month periods ended September 30, 2010. The Company's consolidated financial statements include the results of operations of Delve from the date of acquisition. The historical results of operations of Delve were not significant to the Company's consolidated results of operations for the periods presented. The total purchase consideration was allocated to the assets acquired and liabilities assumed at their estimated fair values as of the date of acquisition, as determined by management. In addition, management has made a preliminary estimate of unidentified intangible assets. The allocation is preliminary and we expect it will be finalized during the fourth quarter of 2010. The excess of the purchase price over the amounts allocated to assets acquired and liabilities assumed has been recorded as goodwill. In accordance with current accounting standards, goodwill associated with the Delve acquisition will not be amortized and will be tested for impairment at least annually (see Note 6). As of September 30, 2010, the Company has recorded approximately \$0.5 million of contingent consideration based on current estimates to achieve the financial milestones in the earn-out provision.

The following table presents the preliminary allocation of the purchase price for Delve:

	(In thousands)
<b>Consideration:</b>	
Cash	\$ 2,810
Common stock	1,428
Total consideration	\$ 4,238
<b>Acquisition-related costs (included in general and administrative expenses)</b>	<b>\$ 150</b>
<b>Recognized amounts of identifiable assets acquired and liabilities assumed:</b>	
Financial assets	\$ 134



Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Property and equipment	12
Unidentified estimated intangible assets	1,682
Financial liabilities	(345)
Total identifiable net assets	1,483
Goodwill	2,755
	\$ 4,238

**Table of Contents**

The total weighted average amortization period for the unidentified estimated intangible assets acquired from Delve is 3.0 years. The goodwill resulting from the Delve acquisition is not deductible for income tax purposes.

**4. Accounts Receivable**

Accounts receivable include (in thousands):

	As of September 30, 2010	As of December 31, 2009
Accounts receivable	\$ 39,631	\$ 29,457
Unbilled accounts receivable	6,945	6,132
	46,576	35,589
Less: credit allowance	(1,150)	(1,190)
Less: allowance for bad debt	(6,341)	(8,036)
Total accounts receivable, net	\$ 39,085	\$ 26,363

**5. Prepaid Expenses and Other Current Assets**

Prepaid expenses and other current assets include (in thousands):

	As of September 30, 2010	As of December 31, 2009
Prepaid bandwidth and backbone services	\$ 3,562	\$ 3,511
Non-income taxes receivable (VAT)	1,485	3,449
Employee advances and prepaid recoverable commissions	279	147
Interest receivable	145	413
Other	3,420	2,134
Total prepaid expenses and other current assets	\$ 8,891	\$ 9,654

The Company is subject to and has paid Value Added Tax (VAT) in certain foreign jurisdictions in which it operates. Based on analysis and application of the VAT laws in particular locations, the Company believes it is entitled to a refund of VAT previously paid.

In January and September 2009, the Company entered into multi-year arrangements with a telecommunications provider for additional bandwidth and backbone capacity. The agreements required the Company to make advanced payments for future services to be received.

**6. Goodwill and Other Intangible Assets**

The Company has recorded goodwill and other intangible assets as a result of its business acquisitions of Kiptronic Inc. (Kiptronic), Chors, EyeWonder and Delve that occurred in May 2009, January 2010, April 2010 and July 2010, respectively.

The excess of the purchase price over the amounts allocated to assets acquired and liabilities assumed has been recorded as goodwill. As of September 30, 2010, the Company has recorded goodwill of approximately \$98.0 million.

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

The Company reviews goodwill for impairment annually or whenever events or changes in circumstances indicate that the carrying amount may exceed their fair value. The Company concluded that it had one reporting unit and assigned the entire balance of goodwill to this reporting unit as of September 30, 2010.

Other intangible assets that are subject to amortization consist of the following (in thousands):

	September 30, 2010		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Existing technologies	\$ 16,580	\$ (1,963)	\$ 14,617
Trademark	1,807	(1)	1,806
Non-compete agreements	1,201	(225)	976

**Table of Contents**

	September 30, 2010		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Patents	789	(82)	707
Usage contract	363	(146)	217
Customer relationships	12	(12)	
Domain names	11	(11)	
Unidentified estimated intangible assets	1,682	(93)	1,589
Total other intangible assets	\$ 22,445	\$ (2,533)	\$ 19,912

  

	December 31, 2009		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Existing technologies	\$ 440	\$ (74)	\$ 366
Domain names	11	(7)	4
Customer relationships and contracts	12	(12)	
Total other intangible assets	\$ 463	\$ (93)	\$ 370

Aggregate expense related to amortization of other intangible assets for the three months ended September 30, 2010 and 2009 was approximately \$1.4 million and \$0.1 million, respectively. For the nine months ended September 30, 2010 and 2009, aggregate expense related to amortization of other intangible assets was approximately \$2.4 million and \$0.1 million, respectively. Based on the Company's other intangible assets as of September 30, 2010, aggregate expense related to amortization of other intangible assets is expected to be \$1.4 million for the remainder of 2010, and \$5.5 million, \$5.2 million, \$4.6 million and \$1.3 million for fiscal years 2011, 2012, 2013 and 2014, respectively.

**7. Property and Equipment**

Property and equipment include (in thousands):

	As of September 30, 2010	As of December 31, 2009
Network equipment	\$ 143,180	\$ 115,505
Computer equipment	7,398	5,493
Furniture and fixtures	895	691
Leasehold improvements	2,984	2,812
Other equipment	483	473
	154,940	124,974
Less: accumulated depreciation and amortization	(103,155)	(89,450)
Total property and equipment	\$ 51,785	\$ 35,524

**8. Other Assets**

Other assets include (in thousands):

Edgar Filing: Limelight Networks, Inc. - Form 10-Q

	As of September 30, 2010	As of December 31, 2009
Prepaid backbone services	\$ 4,993	\$ 7,413
Vendor deposits and other	1,953	719
Restricted cash	314	
Cost basis investments	260	
<b>Total other assets</b>	<b>\$ 7,520</b>	<b>\$ 8,132</b>

In January and September 2009, the Company entered into multi-year arrangements with a telecommunications provider for additional bandwidth and backbone capacity. The agreements required the Company to make advanced payments for future services to be received.

**Table of Contents**

The Company secures its capital lease obligation with a letter of credit that is collateralized by \$263,000 of cash as of September 30, 2010. Upon repayment of the capital lease obligation, the letter of credit would no longer be required and the restricted cash would be available for general use. In addition, the Company secures a business credit card with a letter of credit that is collateralized by approximately \$50,000 of cash that the Company also considers as restricted cash.

On May 18, 2010, the Company made a strategic investment in Gaikai, a private cloud-based gaming technology company that allows users to play major PC and console games through a web browser. The Company will provide services to Gaikai, which will be recorded as revenue when earned, with a corresponding increase in its cost basis of its investment.

**9. Other Current Liabilities**

Other current liabilities consist of the following (in thousands):

	As of September 30, 2010	As of December 31, 2009
Accrued compensation and benefits	\$ 4,943	\$ 2,827
Contingent consideration liability	3,582	
Accrued legal fees	2,721	2,702
Accrued cost of revenue	2,287	2,822
Income taxes payable	1,760	1,905
Non income taxes payable	879	747
Other accrued expenses	3,292	3,137
 Total other current liabilities	 \$ 19,464	 \$ 14,140

The Company has determined that certain transactions are subject to sales tax in some of the states in which it operates. Accordingly, the Company has recorded a liability for those amounts which are probable and reasonably estimated.

**10. Litigation**

In June 2006, Akamai Technologies, Inc., or Akamai, and the Massachusetts Institute of Technology, or MIT, filed a lawsuit against the Company in the United States District Court for the District of Massachusetts alleging that the Company was infringing two patents assigned to MIT and exclusively licensed by MIT to Akamai, United States Patent No. 6,553,413 (the 413 patent) and United States Patent No. 6,108,703 (the 703 patent). In September 2006, Akamai and MIT expanded their claims to assert infringement of a third, recently issued patent United States Patent No. 7,103,645 (the 645 patent). In February 2008, a jury returned a verdict in this lawsuit, finding that the Company infringed four claims of the 703 patent at issue and rejecting the Company's invalidity defenses for the period April 2005 through December 31, 2007. The jury awarded an aggregate of approximately \$45.5 million which includes lost profits, reasonable royalties and price erosion damages. In addition, the jury awarded prejudgment interest which the Company estimated to be \$2.6 million at December 31, 2007. The Company recorded an aggregate \$48.1 million as a provision for litigation as of December 31, 2007. During the year ended December 31, 2008, the Company estimated its revenue from alleged infringing methods totaled approximately 25% of total revenue. The Company recorded a potential additional provision for litigation totaling \$15.5 million, plus additional interest of \$2.0 million, for the year ended December 31, 2008. The total provision for litigation at December 31, 2008 was \$65.6 million.

On July 1, 2008, the court denied the Company's Motions for Judgment as a Matter of Law (JMOL), Obviousness, and a New Trial. The court also denied Akamai's Motion for Permanent Injunction as premature and its Motions for Summary Judgment regarding the Company's equitable defenses. The court conducted a bench trial in November 2008 regarding the Company's equitable defenses. The Company also filed a motion for reconsideration of the court's earlier denial of the Company's motion for JMOL. The Company's motion for JMOL was based largely upon a clarification in the standard for a finding of joint infringement articulated by the Federal Circuit in the case of *Muniauction, Inc. v. Thomson Corp.* (the *Muniauction Case*), released after the court denied the Company's initial motion for JMOL. On April 24, 2009 the court issued its order and memorandum setting aside the adverse jury verdict and ruling that the Company did not infringe Akamai's 703 patent and that the Company is entitled to judgment as a matter of law. Based upon the court's April 24, 2009 order the Company has reversed the \$65.6 million

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

provision for litigation previously recorded for this lawsuit as the Company no longer believes that payment of any amounts represented by the litigation provision is probable. The court entered final judgment in favor of the Company on May 22, 2009, and Akamai filed its notice of appeal of the court's decision on May 26, 2009 and its appeal brief on September 15, 2009 with the United States Court of Appeals for the Federal Circuit. The Company filed its reply brief on December 9, 2009 and each party has filed further appeal briefs. The court heard arguments by both parties on June 7, 2010. The Company intends to vigorously defend the action should the court rule in Akamai's favor. The Company is not able at this time to estimate the range of potential loss nor, in light of the favorable court order, does it believe that a loss is probable. Therefore, there is no provision for this lawsuit in the Company's financial statements.

**Table of Contents**

Legal and other expenses associated with this case have been significant. The Company includes these litigation expenses in general and administrative expenses, as reported in its consolidated statement of operations. The Company expects that the litigation will continue to be expensive, time consuming and a distraction to its management in operating its business.

In December 2007, Level 3 Communications, LLC, or Level 3, filed a lawsuit against the Company in the United States District Court for the Eastern District of Virginia alleging that the Company was infringing certain patents Level 3 acquired from Savvis Communications Corp. In addition to monetary relief, including treble damages, interest, fees and costs, the complaint sought an order permanently enjoining the Company from conducting its business in a manner that infringed the relevant patents. A jury trial was conducted in the United States District Court for the Eastern District of Virginia in January 2009, and on January 23, 2009 the jury returned a verdict favorable to the Company finding that the Company did not infringe the Level 3 patents. The Company believes the jury verdict finding that the Company did not infringe the Level 3 patents is correct, and that the claims of infringement asserted against the Company by Level 3 in the litigation were without merit. The court denied Level 3's subsequent motion for JMOL or alternatively for a new trial, and entered judgment in favor of the Company. Level 3 filed its notice of appeal of the court's decision on July 21, 2009 and its appeal brief on October 5, 2009 with the United States court of Appeals for the Federal Circuit. The Company filed its reply brief on January 19, 2010. On May 3, 2010 the United States Court of Appeals for the Federal Circuit heard oral argument on this matter, and on May 5, 2010 the court affirmed the District Court judgment in favor of the Company. Level 3 subsequently filed a motion for re-hearing and hearing *en banc* that the Court subsequently denied. In light of the favorable ruling the Company does not believe a loss is probable. Therefore, there is no provision for this lawsuit in the Company's financial statements.

In August 2007, the Company, certain of its officers and current and former directors, and the firms that served as the lead underwriters in the Company's initial public offering were named as defendants in several purported class action lawsuits filed in the United States District Courts for the District of Arizona and the Southern District of New York. All of the New York cases were transferred to Arizona and consolidated into a single action. The plaintiffs' consolidated complaint asserted causes of action under Sections 11, 12, and 15 of the Securities Act of 1933, as amended, on behalf of a purported class of individuals who purchased the Company's common stock in its initial public offering and/or pursuant to its Prospectus. The complaint alleges, among other things, that the Company omitted and/or misstated certain facts concerning the seasonality of its business and the loss of revenue related to certain customers. On March 17, 2008, the Company and the individual defendants moved to dismiss all of the plaintiffs' claims and a hearing was held on June 16, 2008. On August 8, 2008, the court granted the motion to dismiss, dismissing plaintiffs' claims under Section 12 with prejudice and granting leave to amend the claims under Sections 11 and 15. Plaintiffs chose not to amend the claims under Sections 11 and 15, and on August 29, 2008 the court entered judgment in favor of the Company. On September 5, 2008, plaintiffs filed a notice of appeal, and appellate briefs were filed by the parties in January and February 2009. The Company believes that it and the individual defendants have meritorious defenses to the plaintiffs' claims and intends to contest the lawsuits vigorously. In November 2009 the parties entered into a Memorandum of Understanding to settle this lawsuit for an amount well within the coverage limits of the primary carrier of our directors and officers liability insurance. The Company is working to finalize the settlement which will require court approval. The Company is not able at this time to estimate the range of potential loss nor, in light of the pending settlement does it believe that a loss is probable. Therefore, there is no provision for these lawsuits in the Company's financial statements.

**11. Net Income (Loss) Per Share**

The Company calculates basic and diluted earnings per share based on income available to common stockholders, which approximates net income for each period, and includes the restricted stock as participating securities. The Company uses the weighted-average number of common shares outstanding during the period, plus the restricted stock discussed above, for the computation of basic earnings per share using the two-class method. Diluted earnings per share include the dilutive effect of convertible stock options and restricted stock units in the weighted-average number of common shares outstanding.

The following table sets forth the components used in the computation of basic and diluted net income (loss) per share for the periods indicated (in thousands, except per share data):

	<b>For the Three Months Ended September 30,</b>		<b>For the Nine Months Ended September 30,</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
Net (loss) income available to common stockholders	\$ (5,954)	\$ (5,220)	\$ (14,004)	\$ 44,617



## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Basic weighted average common shares	98,634	84,489	92,547	84,012
Basic weighted average common shares	98,634	84,489	92,547	84,012
Dilutive effect of stock options and restricted stock units				3,696
Diluted weighted average common shares	98,634	84,489	92,547	87,708

**Table of Contents**

	For the Three Months Ended September 30, 2010		For the Nine Months Ended September 30, 2009	
Basic net (loss) income per share	\$ (0.06)	\$ (0.06)	\$ (0.15)	\$ 0.53
Diluted net (loss) income per share	\$ (0.06)	\$ (0.06)	\$ (0.15)	\$ 0.51

For the three and nine month periods ended September 30, 2010 and the three month period ended September 30, 2009, an aggregate of approximately 4,369,000, 4,551,000 and 4,048,000 respectively, of outstanding options and common stock subject to repurchase were excluded from the computation of diluted net loss per common share because including them would have had an antidilutive effect.

**12. Comprehensive (Loss) Income**

The following table presents the calculation of comprehensive income (loss) and its components (in thousands):

	For the Three Months Ended September 30, 2010		For the Nine Months Ended September 30, 2009	
Net (loss) income	\$ (5,954)	\$ (5,220)	\$ (14,004)	\$ 44,617
Other comprehensive (loss) income, net of tax:				
Unrealized gain on investments	1,015	16	686	118
Foreign exchange translation	923	(1)	(29)	(275)
Other comprehensive income (loss)	1,938	15	657	(157)
Comprehensive (loss) income	\$ (4,016)	\$ (5,205)	\$ (13,347)	\$ 44,460

For the periods presented, accumulated other comprehensive income consisted of (in thousands):

	As of September 30, 2010	As of December 31, 2009
Net unrealized gain on investments, net of tax	\$ 779	\$ 93
Foreign currency translation	(29)	
Total accumulated other comprehensive income	\$ 750	\$ 93

**13. Stockholders Equity**

On January 27, 2010, the Company completed its acquisition of Chors. The aggregate purchase price of Chors including the estimated fair value of the earn-out provision, consisted of approximately \$2.8 million of cash, of which approximately \$2.5 million was paid at closing, and up to 860,000 shares of the Company's common stock, of which 86,000 shares were issued at closing with a determined fair value of approximately \$0.3 million. The fair value of the common stock issued as consideration for Chors was determined on the basis of the closing market price of the Company's common shares on the acquisition date.

On April 30, 2010, the Company completed its acquisition of EyeWonder. The former holders of EyeWonder securities that were outstanding immediately prior to the completion of the acquisition received, in the aggregate, approximately \$49.6 million in cash and 9,726,301 shares of the Company's common stock with a determined value of approximately \$39.1 million based on the closing price of the Company's common

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

stock on April 30, 2010. In addition, the former EyeWonder securityholders may receive up to 4,774,000 shares of the Company's common stock and approximately \$0.3 million in cash in April 2011 if certain performance metrics are satisfied. At this time, the Company does not believe that the performance metrics will be achieved and accordingly has not recorded any contingent consideration. In accordance with the terms of the acquisition, 3,013,699 shares of the Company's common stock have been set aside in an escrow account and will be held until June 28, 2011, subject to any unresolved indemnification claims.

On July 30, 2010, the Company completed its acquisition of Delve. The aggregate purchase price, including the earn-out provision consisted of approximately \$2.8 million of cash and 335,195 shares of the Company's common stock with an estimated fair value of approximately \$1.4 million. The fair value of the common shares issued as consideration for Delve was determined on the basis of the closing market price of the Company's common shares on the acquisition date.

**Table of Contents****14. Share-Based Compensation**

The following table summarizes the components of share-based compensation expense included in the Company's condensed consolidated statement of operations for the three and nine month periods ended September 30, 2010 and 2009 in accordance with current accounting standards (in thousands):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
<b>Share-based compensation expense by type of award:</b>				
Stock options	\$ 2,665	\$ 2,255	\$ 7,672	\$ 6,324
Restricted stock awards and units	1,889	2,114	5,386	6,813
<b>Total share-based compensation expense</b>	<b>\$ 4,554</b>	<b>\$ 4,369</b>	<b>\$ 13,058</b>	<b>\$ 13,137</b>
<b>Effect of share-based compensation expense on:</b>				
Cost of services	\$ 645	\$ 638	\$ 1,827	\$ 1,772
General and administrative expense	1,779	1,805	5,190	5,755
Sales and marketing expense	1,311	1,293	3,789	3,734
Research and development expense	819	633	2,252	1,876
<b>Total cost related to share-based compensation expense</b>	<b>\$ 4,554</b>	<b>\$ 4,369</b>	<b>\$ 13,058</b>	<b>\$ 13,137</b>

Unrecognized share-based compensation expense totaled \$31.0 million at September 30, 2010. The Company expects to amortize \$4.5 million during the remainder of 2010, \$13.1 million in 2011 and the remainder thereafter based upon the scheduled vesting of the stock options, restricted stock awards and units outstanding at that time.

In November 2008, the Company entered into an Equity Award Amendment with the Company's Chief Executive Officer (CEO). In connection with this award, 750,000 options to purchase common stock were cancelled and another 750,000 options were modified. In exchange, the CEO received 500,000 Restricted Stock Units, or RSUs of which 100,000 are service awards vesting over two years and the remaining 400,000 are performance awards. Accordingly, the Company measured the incremental fair value of the RSUs issued over the fair value of the options cancelled and modified and calculated there to be \$317,500 of additional unrecognized share-based compensation which will be recognized over the vesting period of the modified options and RSUs granted.

The performance based RSUs vested if the Company exceeded specified revenue and cash gross margin targets during the quarters ending on or before March 31, 2010. The RSUs are separated into four tranches of 100,000 Performance RSUs each. The maximum number of performance-based RSUs that may vest is based on the achievement of specific quarterly financial targets. Any Performance RSUs that did not vest based on the achievement of the quarterly financial targets with respect to quarters on or before March 31, 2010, expired and were cancelled immediately following the determination of the Company's financial performance for the quarter ending March 31, 2010. As of March 31, 2010, 100,000 of the performance RSUs had vested. The remaining 300,000 performance RSUs expired and have been cancelled.

In May 2009, the Company granted 282,168 performance-based RSUs to various employees. The performance-based RSUs will only vest if a specific revenue target is achieved in any one quarter during the ten full quarters following the date of the grant and provided the employee remains with the Company through the vesting date. As of September 30, 2010, the performance requirement was not probable of being achieved and accordingly no compensation expense has been recognized.

On June 1, 2009, the Company granted 230,000 performance-based RSUs to certain executive officers. Each of the RSU awards, if eligible, shall vest in three (3) equal annual installments beginning on the third business day following the Company's public announcement of its earnings for the fiscal quarter ending June 30, 2010, and the second and third installments vesting on June 1, 2011 and June 1, 2012, provided the executive officer remains with the Company through each such vesting date. All or a portion of the RSUs may become eligible for vesting based upon the achievement of certain financial performance targets for the twelve-month period ending June 30, 2010. RSUs that do not

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

become eligible are forfeited. As of June 30, 2010, 90% of the RSUs became eligible for vesting based on the achievement of the financial performance targets.

On June 1, 2009, the Company granted 320,000 stock options to certain executive officers. Each of the stock option awards vest one quarter (1/4th) on June 1, 2010, and one forty-eighth (1/48th) each month thereafter on the first day of each month, provided the executive officer remains with the Company through each such vesting date.

---

**Table of Contents**

On February 26, 2010, the Company granted 1,850,000 stock options to certain executive officers. Each of the stock option awards vest one forty-eighth (1/48th) on February 1, 2010, and one forty-eighth (1/48th) each month thereafter on the first day of each month, provided the executive officer remains with the Company through each such vesting date.

On February 26, 2010, the Company granted 300,000 performance-based RSUs to the Company's CEO. The RSUs granted to the CEO (and not forfeited) will vest in three tranches, the first of which will vest on the third business day following the release of the Company's fiscal 2010 financial results, the second of which will vest on December 31, 2011 and the third of which will vest on December 31, 2012; provided that the CEO remains an employee or service provider of the Company on each vesting date. All or a portion of the RSUs may become eligible for vesting based upon the achievement of certain financial performance targets related to the earn-out feature described in the Agreement and Plan of Merger to acquire EyeWonder, Inc., a copy of which was filed with a Current Report on Form 8-K on December 21, 2009. RSUs that do not become eligible are forfeited. Each RSU represents a contingent right to receive one (1) share of the Company's common stock. As of September 30, 2010, the performance requirement was not probable of being achieved and accordingly no compensation expense has been recognized.

On April 30, 2010, in connection with the acquisition of EyeWonder, the Company granted 750,000 RSUs to an executive officer and member of its board of directors. The RSUs vest in equal quarterly installments over a period of four years subject to the individual's continued service with the Company.

On April 30, 2010, in connection with the acquisition of EyeWonder, the Company granted 250,000 RSUs to a member of its board of directors, of which 197,500 RSUs were later assigned to eValue AG pursuant to a Consulting Services Agreement with the Company. The RSUs vest in equal quarterly installments over a period of four years subject to continued service to the Company through each vesting date.

**15. Related Party Transactions**

The Company leased office space from a company owned by one of the Company's executives. Rent expense for the lease, including reimbursement for telecommunication lines, was approximately \$0- and \$3,000, respectively, for each of the three month periods ended September 30, 2010 and 2009. For the nine month periods ended September 30, 2010 and 2009, rent expense for the lease including reimbursement for telecommunication lines, was approximately \$4,000 and \$9,000, respectively. In addition, the Company leases office space from an entity in which a member of our executive staff and a member of our board of directors have an ownership interest and are members of the board of directors. During the three and nine month periods ending September 30, 2010, the Company paid approximately \$12,535 to this entity for office space rental.

The Company sells services to entities owned, in whole or in part, by members of the Company's executive staff and board of directors. Revenue derived from related parties was less than 1% of total revenue for the three and nine month periods ended September 30, 2010. For the three and nine month periods ended September 30, 2009, the Company did not generate any revenue from related parties.

**16. Concentrations**

For the three and nine month periods ended September 30, 2010, the Company did not have any customer for which revenue exceeded 10% of total revenue. For the three and nine month periods ended September 30, 2009, the Company had one major customer for which revenue exceeded 10% of total revenue. Revenues for the three and nine month periods ended September 30, 2009, for this customer totaled approximately \$4.8 million and \$15.1 million, respectively.

Revenue from sources outside North America totaled approximately \$15.1 million and \$7.3 million respectively, for the three month periods ended September 30, 2010 and 2009, respectively. Revenue from sources outside North America totaled approximately \$37.6 million and \$20.0 million respectively, for the nine month periods ended September 30, 2010 and 2009, respectively.

**17. Income taxes**

The Company accounts for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. Based upon our estimated annual effective tax rate and discrete

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

items, our estimated tax expense/(benefit) for the three and nine month periods ended September 30, 2010 was approximately \$0.3 million and (\$4.6) million, respectively. For the three and nine month periods ended September 30, 2009 we had a tax expense of approximately \$0.1 million and \$0.6 million, respectively.

The Company records net deferred tax assets to the extent it believes these assets will more likely than not be realized. In making such determination, the Company considers all available positive and negative evidence, including scheduled reversals of

**Table of Contents**

deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial operations. In the event the Company was to determine that it would be able to realize the deferred income tax assets in the future in excess of its net recorded amount, the Company would make an adjustment to the valuation allowance which would reduce the provision for income taxes.

During the nine months ended September 30, 2010, we performed an assessment of the recoverability of deferred tax assets. As a result of the acquisition of EyeWonder, \$5.8 million of net deferred tax liabilities were recorded resulting from the temporary differences generated by the differences between the fair value of assets and liabilities acquired (mainly intangible assets such as existing technologies) and their corresponding tax bases. We determined that \$5.8 million of our pre-acquisition deferred tax assets that had a full valuation allowance are now more-likely-than-not to be realized as a result of the acquisition by offsetting such deferred tax assets against the \$5.8 million net deferred tax liabilities recorded as of the acquisition date. Therefore, we recorded a tax benefit of \$5.8 million related to the partial release of the related valuation allowance. For the remaining balance of deferred tax assets, there was sufficient negative evidence as a result of our cumulative losses to conclude that it was more likely than not that our deferred tax assets would not be realized and we accordingly maintained the remaining valuation allowance. Related to the Chors and Kiptronic acquisitions, we also have certain taxable temporary differences related to intangible assets that cannot be offset by existing deductible temporary differences resulting in a deferred tax liability of approximately \$602,000.

As of September 30, 2010, the Company has approximately \$0.4 million of total unrecognized tax benefits. This total of unrecognized tax benefits, if recognized, would favorably affect the effective income tax rate. Unrecognized tax benefits decreased by \$248,000 during the three months ended September 30, 2010 as a result of payments made in certain foreign jurisdictions. The Company anticipates its unrecognized tax benefits will continue to decrease within twelve months of the reporting date, as a result of settling potential tax liabilities in certain foreign jurisdictions.

The Company recognizes interest and penalties related to unrecognized tax benefits in its tax provision. As of September 30, 2010, the Company has recorded a liability of approximately \$0.3 million for the payment of interest and penalties, which did not materially change during the third quarter of 2010.

The Company files income tax returns in jurisdictions with varying statutes of limitations. Tax years 2006 through 2009 generally remain subject to examination by federal and most state tax authorities. As of September 30, 2010, the Company is not under any Federal examination.

**18. Segment Reporting**

The Company operates in one industry segment – content delivery network services. The Company operates in three geographic areas – North America, EMEA and Asia Pacific.

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. The Company's chief operating decision maker is its Chief Executive Officer. The Company's Chief Executive Officer reviews financial information presented on a consolidated basis for purposes of allocating resources and evaluating financial performance. The Company has one business activity and there are no segment managers who are held accountable for operations, operating results and plans for products or components below the consolidated unit level. Accordingly, the Company reports as a single operating segment.

Revenue by geography is based on the location of the customer from which the revenue is earned. The following table sets forth revenue and long-lived assets by geographic area (in thousands):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Domestic revenue	\$ 34,673	\$ 25,221	\$ 90,445	\$ 78,019
International revenue	15,130	7,309	37,639	20,019
<b>Total revenue</b>	<b>\$ 49,803</b>	<b>\$ 32,530</b>	<b>\$ 128,084</b>	<b>\$ 98,038</b>

The following table sets forth long-lived assets by geographic area (in thousands):

As of September 30, 2010	As of December 31, 2009
--------------------------------	-------------------------------



Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Domestic long-lived assets	\$	34,031	\$	20,889
International long-lived assets		17,754		14,635
Total long-lived assets	\$	51,785	\$	35,524

**Table of Contents****19. Fair Value Measurements**

The Company evaluates certain of its financial instruments within the three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include:

- Level 1 defined as observable inputs such as quoted prices in active markets;
- Level 2 defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and
- Level 3 defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

As of September 30, 2010, the Company held certain assets and liabilities that are required to be measured at fair value on a recurring basis. These include corporate notes and bonds and US Government Agency Bonds, publicly traded stocks, and private equity securities which are classified as marketable securities and acquisition related contingent consideration which is classified as a current liability on the Company's condensed consolidated balance sheet.

The following is a summary of marketable securities, other investment-related assets and current liabilities held at September 30, 2010 (in thousands):

Description	Total	Fair Value Measurements at Reporting Date Using		
		Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>				
Government agency bonds	\$ 11,340	\$ 11,340	\$	\$
Corporate notes and bonds	7,081	7,081		
Private equity security	260			260
Publicly traded common stock	2,024	2,024		
<b>Total assets measured at fair value</b>	<b>\$ 20,705</b>	<b>\$ 20,445</b>	<b>\$</b>	<b>\$ 260</b>
<b>Liabilities:</b>				
Acquisition related contingent consideration	\$ 3,582	\$	\$	\$ 3,582
<b>Total liabilities measured at fair value</b>	<b>\$ 3,582</b>	<b>\$</b>	<b>\$</b>	<b>\$ 3,582</b>

For the period ended September 30, 2010, realized gains and losses for marketable securities are reported in interest income, unrealized gains and losses for marketable securities are included in other comprehensive income and expense. For the nine month period ended September 30, 2010, the Company had net unrealized gains of approximately \$774,000.

On January 27, 2010, the Company acquired chors. The total consideration included contingent consideration of up to \$3.1 million upon the achievement of certain financial milestones. On the acquisition date, a liability was recognized for an estimate of the acquisition date fair value of the contingent financial milestone consideration based on the probability of achieving the financial milestones and the probability weighted discount on cash flows. At this time the Company believes that the financial milestones will be achieved and did not discount the contingent consideration. Future changes in fair value of the contingent financial milestone consideration, as results of changes in significant inputs such as the discount rate and estimated probabilities of financial milestone achievements, could have a material effect on the statement of operations and

financial position in the period of the change.

On May 18, 2010, the Company made a strategic investment in Gaikai, a private cloud-based gaming technology company that allows users to play major PC and console games through a web browser. The Company will provide services to Gaikai, which will be recorded as revenue when earned, with a corresponding increase in its cost basis of its investment.

On July 30, 2010, the Company acquired Delve. The total consideration included contingent consideration of up to \$0.5 million upon the achievement of certain financial milestones. On the acquisition date, a liability of \$0.5 million was recognized for an estimate of the acquisition date fair value of the contingent financial milestone consideration based on the probability of achieving the financial milestones and the probability weighted discount on cash flows. At this time the Company believes that the financial milestones will be achieved and did not discount the contingent consideration. Future changes in fair value of the contingent financial milestone consideration, as results of changes in significant inputs such as the discount rate and estimated probabilities of financial milestone achievements, could have a material effect on the statement of income and financial position in the period of the change.

**Table of Contents**

The fair value measurement for both the contingent consideration and the private equity security is based on significant inputs not observed in the market and thus represents a Level 3 measurement. Level 3 instruments are valued based on unobservable inputs that are supported by little or no market activity and reflect the Company's own assumptions in measuring fair value.

The progressions of the Company's Level 3 instruments for the three months ended September 30, 2010 are shown in the table below (in thousands):

	Acquisition Related Contingent Consideration	Private Equity Securities
Balance at June 30, 2010	\$ 3,054	\$ 66
Additions	500	194
Change in value	28	
Total assets measured at fair value	\$ 3,582	\$ 260

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

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements and the related notes thereto included elsewhere in this quarterly report on Form 10-Q and the audited consolidated financial statements and notes thereto and management's discussion and analysis of financial condition and results of operations for the year ended December 31, 2009 included in our annual report on Form 10-K filed with the Securities and Exchange Commission, or SEC, on March 12, 2010. This quarterly report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements include statements as to industry trends and future expectations of ours and other matters that do not relate strictly to historical facts. These statements are often identified by the use of words such as may, will, expect, believe, anticipate, intend, could, estimate, or continue, and similar expressions or variations. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled Risk Factors set forth in Part II, Item 1A of this quarterly report on Form 10-Q and in our other SEC filings. We undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements. Prior period information has been modified to conform to current year presentation.*

**Overview**

We were founded in 2001 as a provider of content delivery network, or CDN, services to deliver digital content over the Internet. We began development of our infrastructure in 2001 and began generating meaningful revenue in 2002. In May 2009, January 2010, April 2010 and July 2010, respectively, we acquired Kiptronic, chors, EyeWonder and Delve. Today, Limelight Networks provides on-demand software, platform, and infrastructure services that help global businesses reach and engage audiences on any mobile or connected device, enabling them to enhance their brand presence, build stronger customer relationships, manage video assets, analyze viewer preferences, optimize their advertising, and monetize their digital assets. We provide services to customers in the North America, EMEA, and the Asia Pacific region. As of September 30, 2010, we had approximately 1,780 active customers worldwide. We derive revenue from the sale of services to our customers. These services include the delivery of digital media, including video, music, games, software and social media, the acceleration of web sites and web-based applications, and value-added services such as mobility, interactive advertising, computing, storage, data center, transit, and consulting. We operate in one business segment. Our CDN customers normally execute contracts with terms of one year or longer, which we refer to as recurring revenue contracts or long-term contracts. These contracts generally commit the customer to a minimum monthly level of usage with additional charges applicable for actual usage above the monthly minimum commitment. We have entered into an increasing number of customer contracts that have minimum usage commitments that are based on twelve-month or longer periods and in some cases, other arrangements. We believe that having a consistent and predictable base level of revenue is important to our financial success. Accordingly, to be

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

successful, we must maintain our base of recurring revenue contracts by eliminating or reducing any customer cancellations or terminations and build on that base by adding new customers and increasing the number of services, features and functionalities our existing customers purchase. We also derive revenue from campaigns, services and events sold as discrete, non-recurring events or based solely on usage. For these services, we recognize revenue after an enforceable contract has been signed by both parties, the fee is fixed or determinable, the event or usage has occurred and collection is reasonably assured.

On July 30, 2010 the Company acquired Delve Networks, Inc. (Delve), a privately-held provider of cloud-based video publishing and analytics services located in Seattle, Washington. The aggregate purchase price, including the earn-out provision, consisted of approximately \$2.8 million of cash and 335,195 shares of the Company's common stock with an estimated fair value of

**Table of Contents**

approximately \$1.4 million. The fair value of the common shares issued as consideration for Delve was determined on the basis of the closing market price of the Company's common shares on the acquisition date. Our consolidated financial statements include the results of operations of Delve from the date of acquisition. The historical results of operations of Delve were not significant to our consolidated results of operations for the periods presented.

On April 30, 2010, we completed the acquisition of EyeWonder. The aggregate purchase price, excluding the earn-out provision consisted of approximately \$62.8 million of cash and 12,740,000 shares of our common stock with an estimated fair value of approximately \$51.2 million. Under the terms of the Merger Agreement, the former holders of EyeWonder securities that were outstanding immediately prior to the completion of the merger received, in the aggregate, approximately \$49.6 million in cash and 9,726,301 shares of our common stock with a determined value of approximately \$39.1 million based on the closing price of our common stock on April 30, 2010. In addition, the former EyeWonder securityholders may receive up to 4,774,000 shares of our common stock and approximately \$0.3 million in cash in April 2011 if certain performance metrics are satisfied. At this time, we do not believe that the performance metrics will be achieved and accordingly have not recorded any contingent consideration. Under the terms of the Merger Agreement, 3,013,699 shares of our common stock have been set aside in an escrow account and will be held until June 28, 2011, subject to any unresolved indemnification claims. EyeWonder is a provider of interactive digital advertising products and services to advertisers, advertising agencies and publishers. EyeWonder creates and executes online video and rich media advertising campaigns on behalf of advertisers. EyeWonder was a pioneer in the delivery of video ads online and continues to be a leader in industry innovation, delivering engaging brand experiences across hundreds of online publishers and digital media channels, including online, mobile and in-game, and across a variety of formats. Through its innovative technology, products and services, EyeWonder provides advertisers, advertising agencies and content publishers the ability to create, build, deliver, track and optimize interactive advertising campaigns. EyeWonder's in-page, in-stream and mobile advertising products combine the quality and power of Adobe Flash® video and the latest creative features, as well as online tracking and reporting capabilities to enhance the impact and effectiveness of rich media advertising campaigns. EyeWonder has executed campaigns for hundreds of advertisers across a wide variety of sectors.

EyeWonder was founded in 1999 and is headquartered in Atlanta, Georgia, with offices in New York, Chicago, San Francisco, Dallas, Los Angeles, the United Kingdom, Ireland, the Netherlands, Germany, Spain and Australia. At the time of the acquisition, EyeWonder and its subsidiaries employed a staff of approximately 240.

In January 2010, we acquired chors GmbH, or chors, an on-line and direct marketing solution provider located in Germany. The aggregate purchase price, including the earn-out provision consisted of approximately \$2.8 million of cash and up to 860,000 shares of the Company's common stock with tentative aggregate consideration determined to be approximately \$5.8 million.

During 2007, we entered into a multi-element arrangement which generates revenue by providing consulting services related to the development of a custom CDN solution, through the cross-license of certain technologies, including certain components of our CDN software and technology, and post-contract customer support (PCS) for both the custom CDN-solution and the software component. We also derive some business from the sale of custom CDN services. These are generally limited to modifying our network to accommodate non-standard content player software or to establish dedicated customer network components that reside both within our network or that operate within our customers' network.

Traffic on our network has continued to grow both for the quarter and year to date periods when compared to prior year. This traffic growth is primarily the result of growth in the traffic delivered on behalf of both new and existing customers. Our CDN revenue is generated by charging for traffic delivered. During the quarter ended September 30, 2010, we continued to add new customers, both through new business and through our business acquisitions. We have seen an increase in the length of our sales cycle, but we continue to see that new and existing customers want the benefits of the specialized services that we bring to the market. We are also experiencing continuing pricing pressure, particularly with our larger customers.

Historically, we have derived a portion of our revenue from outside of North America. Our international revenue has grown recently, and we expect this trend to continue as we focus on our strategy of expanding our network and customer base internationally. For the year ended December 31, 2009 revenue derived from customers outside North America accounted for approximately 22% of our total revenue. For the year ended December 31, 2009 we derived approximately 69% of our international revenue from operations in EMEA and approximately 31% of our international revenue from Asia Pacific, respectively. For the three month periods ended September 30, 2010 and 2009, respectively, revenue derived from customers outside North America accounted for approximately 30% and 22% respectively, of our total revenue. For the nine month periods ended September 30, 2010 and 2009 revenue derived from customers outside North America accounted for approximately 29% and 20% respectively, of our total revenue. For the three and nine month periods ended September 30, 2010, we derived approximately 67% and 64%, respectively, of our international revenue from EMEA and approximately 33% and 36%, respectively, of our international revenue from Asia Pacific. We expect foreign revenue as a percentage of our total revenues to increase in 2010. Our international business is managed as a single geographic segment, and we report our financial results on this basis.



---

## Table of Contents

During any given fiscal period, a relatively small number of customers typically account for a significant percentage of our revenue. For example, in 2009, sales to our top 10 customers, in terms of revenue, accounted for approximately 36% of our total revenue. During 2009, one of these top 10 customers, Microsoft, represented approximately 14% of our total revenue for that period. For the three and nine month periods ended September 30, 2010, sales to our top 10 customers, in terms of revenue, accounted for approximately 32% and 30%, respectively of our total revenue. During the three and nine month periods ended September 30, 2010 we had no customer that accounted for more than 10% of our revenue during those periods. We anticipate customer concentration levels will decrease compared to prior years. In addition to selling to our direct customers, we maintain relationships with a number of resellers that purchase our services and charge a mark-up to their end customers. Revenue generated from sales to reseller customers accounted for approximately 2% of our total revenue for the year ended December 31, 2009. For the three and nine month periods ended September 30, 2010, revenue generated from sales to reseller customers was approximately 5%, respectively, of our total revenue.

In addition to these revenue-related business trends, our cost of revenue increased in absolute dollars and decreased as a percentage of revenue for the three and nine month periods ended September 30, 2010 compared to the three and nine month periods ended September 30, 2009. This increase in absolute dollars is primarily the result of increased cost of bandwidth associated with increased traffic on our network, increased co-location fees associated with increased investments to build out the capacity of our network and increased operations personnel resulting from our business acquisitions and additional personnel required to operate our expanding network.

Operating expenses increased in absolute dollars and slightly increased as a percentage of revenue for the three month period ended September 30, 2010 compared to the three month period ended September 30, 2009. This increase was primarily due to increased general and administrative costs (primarily payroll and related employee costs, due to increased staffing primarily due to increased personnel from our business acquisitions and facility and facility related expenses), increased sales and marketing expenses (primarily payroll and related employee costs due to increased staffing primarily due to increased personnel from our business acquisitions) and increased research and development costs (also, primarily payroll and related employee costs due to increased staffing, again primarily due to increased personnel from our business acquisitions) and increased non-network related depreciation and amortization associated with the amortization of acquired intangible assets. For the nine month period ended September 30, 2010, operating expenses increased compared to the nine month period ended September 30, 2009. This increase was primarily due to increased general and administrative costs (primarily payroll and related employee costs, due to increased staffing and facility, additional fees licenses and non-income taxes, and facility related expenses, off-set by lower litigation expenses), increased sales and marketing expenses (primarily payroll and related employee costs due to increased staffing) and increased research and development costs (also, primarily payroll and related employee costs due to increased staffing), and increased non-network related depreciation and amortization associated with the amortization of acquired intangible assets.

We make our capital investment decisions based upon careful evaluation of a number of variables, such as the amount of traffic we anticipate on our network, the cost of the physical infrastructure required to deliver that traffic, and the forecasted capacity utilization of our network. Our capital expenditures have varied over time, in particular as we purchased servers and other network equipment associated with our network build-out. For example, in 2007, 2008 and 2009, we made capital purchases of \$26.5 million, \$20.1 million and \$21.7 million, respectively. For the three and nine month periods ended September 30, 2010, we made capital investments of \$11.7 million and \$25.4 million, respectively. We continue to see improvements in the efficiency of our network allowing us to meet traffic growth with less investment, however, we expect to have ongoing capital expenditure requirements, as we continue to invest in and expand our CDN. For 2010, we currently anticipate making aggregate capital expenditures of approximately 16% to 18% of total revenue for the year.

Occasionally we generate revenue from customers that are entities related to certain of our executives. For the year ended December 31, 2009, we did not generate any revenue from related parties. Revenue derived from related parties was less than 1% of total revenue for the three and nine month periods ended September 30, 2010.

We are currently engaged in litigation with one of our principal competitors, Akamai Technologies, Inc., or Akamai, and its licensor, the Massachusetts Institute of Technology, or MIT, in which these parties have alleged that we are infringing three of their patents. In February 2008, a jury returned a verdict in this lawsuit, finding that we infringed four claims of the patent at issue (United States Patent No. 6,108,703 (the 703 patent) and rejecting our invalidity defenses. The court conducted a bench trial in November 2008, regarding our equitable defenses; and we filed a motion for reconsideration of the court's earlier denial of our motion for Judgment as a Matter of Law (JMOL). Our motion for reconsideration of JMOL was based largely upon a clarification in the standard for a finding of joint infringement articulated by the Federal Circuit in the case of *Muniauction, Inc. v. Thomson Corp.* (the *Muniauction Case*), released after the court denied our initial motion for JMOL. On April 24, 2009 the court issued its order and memorandum setting aside the adverse jury verdict and ruling that we did not infringe Akamai's 703 patent and that we are entitled to judgment as a matter of law. Based upon the court's April 24, 2009 order we reversed the \$65.6 million provision for litigation previously recorded for this lawsuit as we no longer believe that payment of any amounts represented by the litigation provision is probable. The court entered final judgment in favor of us on May 22, 2009, and Akamai filed a notice of appeal on May 26, 2009.



Edgar Filing: Limelight Networks, Inc. - Form 10-Q

and filed its appeal brief on September 15, 2009 with the United States Court of Appeals for the Federal Circuit. We filed our reply brief

---

**Table of Contents**

on December 9, 2009 and each party has filed further appeal briefs. The court heard arguments by both parties on June 7, 2010. We cannot assure you that this lawsuit ultimately will be resolved in our favor. We intend to vigorously defend the action should the court rule in Akamai's favor. Our legal and other expenses associated with this case have been significant. We include these litigation expenses in general and administrative expenses, as reported in our condensed consolidated statement of operations. We expect that these expenses will continue to be significant.

In December 2007, Level 3 Communications, LLC, or Level 3, filed a lawsuit against us in the United States District Court for the Eastern District of Virginia alleging that we were infringing certain patents Level 3 acquired from Savvis Communications Corp. In addition to monetary relief, including treble damages, interest, fees and costs, the complaint sought an order permanently enjoining us from conducting our business in a manner that infringed the relevant patents. A jury trial was conducted in January 2009, and on January 23, 2009 the jury returned a verdict favorable to us finding that we did not infringe the Level 3 patents. We believe the jury verdict finding that we did not infringe the Level 3 patents is correct, and that the claims of infringement asserted against us by Level 3 in the litigation were without merit. The court denied Level 3's subsequent motion for JMOL or alternatively for a new trial, and entered a judgment in our favor. Level 3 filed a notice of appeal on July 21, 2009 and filed its appeal brief on October 5, 2009. We filed our reply brief on January 19, 2010. On May 3, 2010 the United States Court of Appeals for the Federal Circuit heard oral argument on this matter, and on May 5, 2010 the court affirmed the District Court judgment in our favor. Level 3 subsequently filed a motion for re-hearing and hearing *en banc* that the Court subsequently denied. Our legal and other expenses associated with this case have been significant. We include these litigation expenses in general and administrative expenses, as reported in our condensed consolidated statement of operations.

In August 2007, we, certain of our officers and current and former directors, and the firms that served as the lead underwriters in our initial public offering were named as defendants in several purported class action lawsuits filed in the United States District Courts for the District of Arizona and the Southern District of New York. All of the New York cases were transferred to Arizona and consolidated into a single action. The plaintiffs' consolidated complaint asserted causes of action under Sections 11, 12, and 15 of the Securities Act of 1933, as amended, on behalf of a purported class of individuals who purchased our common stock in our initial public offering and/or pursuant to our Prospectus. The complaint alleged, among other things, that we omitted and/or misstated certain facts concerning the seasonality of our business and the loss of revenue related to certain customers. On March 17, 2008, we and the individual defendants moved to dismiss all of the plaintiffs' claims, a hearing was held on this motion on June 16, 2008. On August 8, 2008, the court granted the motion to dismiss, dismissing plaintiffs' claims under Section 12 with prejudice and granting leave to amend the claims under Sections 11 and 15. Plaintiffs chose not to amend the claims under Sections 11 and 15, and on August 29, 2008, the court entered judgment in favor of us. On September 5, 2008 plaintiffs filed a notice of appeal, and appellate briefs were filed by the parties in January and February, 2009. We believe that we and the individual defendants have meritorious defenses to the plaintiffs' claims and intend to contest the lawsuit vigorously. In November 2009 the parties entered into a Memorandum of Understanding to settle this lawsuit for an amount well within the coverage limits of the primary carrier of our directors and officers liability insurance. We are working to finalize the settlement, which will require court approval. At this time we do not believe that a loss is probable. Therefore, there is no provision for this lawsuit in our financial statements.

We were unprofitable for the nine months ended September 30, 2010; significant items impacting our unprofitability were depreciation and amortization expense and share-based compensation expense. For the nine months ended September 30, 2009 we were profitable; the largest impact to our profitability was the reversal of our provision for litigation judgment accrual of \$65.6 million regarding the patent infringement lawsuit filed by Akamai Technologies, Inc.

Our future results will be affected by many factors identified in the section captioned "Risk Factors," in this quarterly report on Form 10-Q, including our ability to:

increase our revenue by adding customers and limiting customer cancellations and terminations, as well as increasing the amount of monthly recurring revenue that we derive from our existing customers;

manage the prices we charge for our services, as well as the costs associated with operating our network in light of increased competition;

successfully manage our litigation with Akamai to a favorable conclusion;

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

prevent disruptions to our services and network due to accidents or intentional attacks; and

continued ability to deliver a significant portion of our traffic through settlement free peering relationships which significantly reduce our cost of delivery.

As a result, we cannot assure you that we will achieve our expected financial objectives, including positive net income.

### **Critical Accounting Policies and Estimates**

Our discussion and analysis of our financial condition and results of operations are based upon our unaudited condensed consolidated financial statements included elsewhere in this quarterly report on Form 10-Q, which have been prepared by us in

**Table of Contents**

accordance with United States generally accepted accounting principles for interim periods. These principles require us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, cash flow and related disclosure of contingent assets and liabilities. Our estimates include, but are not limited to those related to revenue recognition, accounts receivable reserves, income and other taxes, stock-based compensation, equipment, goodwill, intangible assets and contingent obligations. 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. To the extent that there are material differences between these estimates and our actual results, our future financial statements will be affected.

With the exception of the items noted below, as of September 30, 2010, there have been no material changes to any of the critical accounting policies as described in our annual report on Form 10-K for the year ended December 31, 2009, filed with the SEC on March 12, 2010. During the quarterly periods between the February 2008 adverse jury verdict in the patent infringement lawsuit filed by Akamai Technologies, Inc. and the Court's April 24, 2009 order, we had accrued for potential damages and interest. Based upon the Court's April 24, 2009 order we have reversed the \$65.6 million provision for litigation previously recorded for this lawsuit as we no longer believe that payment of any amounts represented by the litigation provision is probable.

In connection with certain of our acquisitions, additional contingent considerations may be earned in the future by the selling entity upon completion of certain financial milestones. Current accounting standards regarding business combinations, for all acquisitions consummated on or after January 1, 2009, require that a liability is recognized on the acquisition date for an estimate of the acquisition date fair value of the contingent consideration based on the probability of achieving the milestones and the probability weighted discount on cash flows. Any change in the fair value of contingent milestone consideration subsequent to the acquisition date is recognized in the consolidated statements of income.

In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2009-13, Revenue Recognition (Topic 605) Multiple-Deliverable Revenue Arrangements. ASU 2009-13 addresses the accounting for multiple-deliverable arrangements to enable vendors to account for products or services (deliverables) separately rather than as a combined unit. Specifically, this guidance amends the criteria in Subtopic 605-25, Revenue Recognition-Multiple-Element Arrangements (Subtopic 605-25), for separating consideration in multiple-deliverable arrangements. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence; (b) third-party evidence; or (c) management's best estimate. This guidance also eliminates the residual method of allocation and requires that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method. In the third quarter of 2010, we early adopted ASU 2009-13 with such adoption being effective for revenue arrangement entered into or materially modified after January 1, 2010. The Company did not enter into or modify any multi-element arrangements falling under the scope of ASU 2009-13 during the six months ended June 30, 2010. We recognized \$1.1 million of revenue related to a multi-element arrangement accounted for in accordance with ASU 2009-13 during the three and nine month periods ended September 30, 2010. In October 2009, the FASB also issued ASU 2009-14, Software (Topic 985) Certain Revenue Arrangements That Include Software Elements. ASU 2009-14 changes revenue recognition for tangible products containing software and hardware elements. Specifically, tangible products containing software and hardware that function together to deliver the tangible products' essential functionality are scoped out of the existing software revenue recognition guidance and will be accounted for under the multiple-element arrangements revenue recognition guidance under ASU 2009-13. In the third quarter of 2010 in conjunction with the adoption of ASU 2009-13, we early adopted ASU 2009-14 with such adoption being effective for revenue arrangement entered into or materially modified after January 1, 2010. We did not enter into or modify any arrangements falling under the scope of ASU 2009-14 during the nine months ended September 30, 2010, and accordingly the impact of adoption was not material to our financial position, results of operations or cash flows.

**Results of Operations****Revenue**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009	Increase (Decrease)	Percent Change	2010	2009	Increase (Decrease)	Percent Change
	(in thousands)				(in thousands)			
Revenue	\$ 49,803	\$ 32,530	\$ 17,273	53%	\$ 128,084	\$ 98,038	\$ 30,046	31%

Revenue increased 53%, or \$17.3 million, to \$49.8 million for the three months ended September 30, 2010 as compared to \$32.5 million for the three months ended September 30, 2009. For the nine months ended September 30, 2010, total revenues increased 31%, or \$30.0 million, to \$128.1 million as compared to \$98.0 million for the nine months ended September 30, 2009. The increase in revenue for the three and nine month periods ended September 30, 2010 as compared to the same periods in the prior year was primarily attributable to an increase in our value added services revenue (which includes revenue from the date of acquisition of Chorus, EyeWonder and Delve) of approximately \$13.2 million

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

and \$23.8 million, respectively. We provide value added services in the following areas: whole and website business portal acceleration, web and enterprise acceleration, mobile content delivery, online and mobile ad serving, rich media ad unit design and creation, cloud storage, transcoding and computing functions and strategic

**Table of Contents**

consulting. We continued to increase the amount of traffic moving through our network; however we continue to see a decline in our average unit sales price. Our core delivery revenue increased approximately \$4.0 million and \$6.2 million, respectively, for the three and nine month periods ended September 30, 2010, compared to the same periods in the prior year. As of September 30, 2010, we had approximately 1,780 customers under revenue contracts as compared to approximately 1,370 as of September 30, 2009.

For the three months ended September 30, 2010 and 2009, approximately 30% and 22%, respectively, of our total revenues were derived from our operations located outside of North America. For the three months ended September 30, 2010 and 2009, we derived approximately 67%, respectively, of our international revenue from EMEA and approximately 33%, respectively, of our international revenue from Asia Pacific. For the nine months ended September 30, 2010 and 2009, approximately 29% and 20%, respectively, of our total revenues were derived from our operations located outside of North America. For the nine months ended September 30, 2010 and 2009, we derived approximately 64% and 71%, respectively, of our international revenue from EMEA and approximately 36% and 29%, respectively, of our international revenue from Asia Pacific. No single country outside of the United States accounted for 10% or more of revenues during these periods.

**Cost of Revenue**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009	Increase (Decrease)	Percent Change	2010	2009	Increase (Decrease)	Percent Change
	(in thousands)				(in thousands)			
Cost of revenue	\$ 27,946	\$ 20,907	\$ 7,039	34%	\$ 72,753	\$ 63,456	\$ 9,297	13%

Cost of revenue includes fees paid to network providers for bandwidth and backbone, costs incurred for non settlement free peering and connection to Internet service provider networks or ISPs, and fees paid to data center operators for co-location of our network equipment. Cost of revenue also includes depreciation of network equipment used to deliver our CDN services, payroll and related costs and equity-related compensation for our network operations, operations and value added services personnel.

Cost of revenue increased 34%, or \$7.0 million, to \$27.9 million for the three months ended September 30, 2010 as compared to \$20.9 million for the three months ended September 30, 2009. These increases were primarily due to an increase in aggregate bandwidth and co-location fees of \$2.1 million due to higher traffic levels and increased amounts of deployed network assets, an increase in payroll and related employee costs of \$3.2 million associated with increased staff to build and operate our CDN, as well as increased operations personnel from our business acquisitions whose primary focus is on our delivery of value added services, an increase in travel and travel related expenses of \$0.1 million, and an increase in other costs of \$1.7 million. The increase in other costs was primarily related to costs associated with value added services and the sale of equipment to one of our customers. These increases were off-set by a reduction in depreciation expense of network equipment of \$0.1 million. For the nine months ended September 30, 2010, cost of revenues increased 13%, or \$9.3 million, to \$72.8 million as compared to \$63.4 million for the nine months ended September 30, 2009. These increases were primarily due to an increase in aggregate bandwidth and co-location fees of \$3.6 million due to higher traffic levels and increased amounts of deployed network assets, an increase in payroll and related employee costs of \$6.4 million associated with increased staff to build and operate our CDN, as well as increased operations personnel resulting from our business acquisitions whose primary focus is on our delivery of value added services, an increase in travel and travel related expenses of \$0.3 million, and an increase in other costs of \$1.9 million. The increase in other costs was primarily related to costs associated with value added services and the sale of equipment to one of our customers. These increases were off-set by a reduction in depreciation expense of network equipment of \$2.7 million.

Additionally, cost of revenue share-based compensation expense remained constant at \$0.6 million for the three month periods ended September 30, 2010 and 2009. For the nine month period ended September 30, 2010, cost of revenue share-based compensation expense remained constant at \$1.8 million compared to the nine month period ended September 30, 2009.

Cost of revenue was composed of the following (in millions):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Bandwidth and co-location fees	\$ 13.1	\$ 11.0	\$ 37.1	\$ 33.5
Depreciation network	5.9	6.0	16.0	18.7

Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Payroll and related employee costs	5.5	2.2	12.7	6.3
Share-based compensation	0.6	0.6	1.8	1.8
Travel and travel-related expenses	0.2	0.1	0.5	0.2
Professional fees and outside services	0.1	0.2	0.5	0.4
Royalty expenses	0.1	0.2	0.2	0.5
Other costs	2.4	0.6	4.0	2.1

**Table of Contents**

	For the Three Months Ended September 30, 2010		For the Nine Months Ended September 30, 2009	
Total cost of revenues	\$ 27.9	\$ 20.9	\$ 72.8	\$ 63.5

We have long-term purchase commitments for bandwidth usage and co-location with various Tier 1 network providers and data center operators. The minimum commitments related to bandwidth usage and co-location services under agreements currently in effect are approximately: \$6.1 million for the remainder of 2010, \$15.6 million for 2011, \$7.4 million for 2012, \$3.5 million for 2013 and \$4.1 million for 2014 and beyond.

We anticipate cost of revenues will increase during the remainder of 2010. We expect to deliver more traffic on our network, which would result in higher expenses associated with the increased rack and co-location costs to support increased traffic; however, such costs are likely to be partially offset by lower bandwidth costs per unit. We anticipate depreciation expense related to our network equipment to decrease compared to 2009 in absolute dollars. Additionally, we expect an increase in payroll and related costs, as we continue to make investments in our network to service our expanding customer base as well as our increase in value added services personnel. The fourth quarter will include a full quarter of activity for Delve, compared to two months of activity during the quarter ended September 30, 2010. We expect that share-based compensation expense will remain consistent with 2009.

**General and Administrative**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009 (in thousands)	Increase (Decrease)	Percent Change	2010	2009 (in thousands)	Increase (Decrease)	Percent Change
General and administrative	\$ 8,359	\$ 6,405	\$ 1,954	31%	\$ 26,095	\$ 24,714	\$ 1,381	6%

General and administrative expenses consist primarily of the following components:

payroll, share-based compensation and other related costs, including related expenses for executive, finance, legal, business applications, internal network management, human resources and other administrative personnel;

fees for professional services and litigation expenses;

rent and other facility-related expenditures for leased properties;

the provision for doubtful accounts; and

non-income related taxes.

General and administrative expenses increased 31%, or \$2.0 million, to \$8.4 million for the three months ended September 30, 2010 as compared to \$6.4 million for the three months ended September 30, 2009. The increase in general and administrative expenses for the three months ended September 30, 2010 compared to the three months ended September 30, 2009 was primarily due to an increase in payroll and related employee costs of \$1.4 million, primarily due to increased personnel resulting from our business acquisitions, an increase in professional fees of \$0.6 million, which was primarily due to increased consulting, acquisition related professional fees, accounting fees and other outside services, an increase in travel and travel related expenses of \$0.2 million, and an increase in other costs of \$0.9 million, primarily due to increased facilities and facilities related costs associated with our business acquisitions of \$0.5 million, increased fees, licenses and non-income taxes of \$0.1 million, increased telephone costs of \$0.2 million and a increase in general office expenses (office and computer supplies, postage and shipping) of approximately \$0.1 million. These increases were off-set by decreases in bad debt of \$0.8 million, due to improved management of our accounts receivable and a decrease in litigation expenses of \$0.3 million. For the nine months ended September 30, 2010, general and administrative expenses increased 6%, or \$1.4 million, to \$26.1 million as compared to \$24.7 million for the nine months ended



## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

September 30, 2009. The increase in general and administrative expenses for the nine months ended September 30, 2010 compared to the nine months ended September 30, 2009 was primarily due to an increase of \$2.7 million in payroll and related employee cost, again primarily due to increased personnel resulting from our business acquisitions, an increase in professional fees of \$0.6 million, primarily acquisition related expenses, off-set by lower accounting and general legal fees, and an increase in other costs of \$2.2 million, again primarily due to increased facilities and facilities related costs of \$0.9 million, increased fees, licenses and non-income taxes of \$0.9 million, increased telephone costs of \$0.3 million and an increase in general office expenses (office and computer supplies, postage and shipping) of approximately \$0.1 million. Other expenses include such items as rent, utilities, telephone, insurance, fees and licenses and property taxes. These increases were off-set by a decrease of \$2.5 million in litigation expenses related to our litigation with Akamai and MIT, and Level 3, and a decrease of \$1.3 million in bad debt expense.

**Table of Contents**

Additionally, general and administrative share-based compensation expense remained constant at \$1.8 million for the three month periods ended September 30, 2010 and 2009, respectively. For the nine month period ended September 30, 2010, share-based compensation decreased \$0.6 million to \$5.2 million, compared to \$5.8 million for the nine month period ended September 30, 2009.

General and administrative expense was composed of the following (in millions):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Payroll and related employee costs	\$ 2.9	\$ 1.5	\$ 7.0	\$ 4.3
Professional fees, legal and outside services	1.9	1.3	4.8	4.2
Share-based compensation	1.8	1.8	5.2	5.8
Travel and travel related	0.3	0.1	0.6	0.3
Litigation expenses		0.3	2.1	4.6
Bad debt expense	(0.6)	0.2	1.3	2.6
Other expenses	2.1	1.2	5.1	2.9
Total general and administrative	\$ 8.4	\$ 6.4	\$ 26.1	\$ 24.7

We expect general and administrative expenses to increase in 2010 in absolute dollars and to decrease as a percentage of revenue. The increase is primarily due to increased payroll and payroll related employee costs due to increased staffing, off-set by lower costs associated with ongoing litigation, as well as decreases in accounting and legal and other costs associated with public reporting requirements and compliance with the requirements of the Sarbanes-Oxley Act of 2002. In addition, the fourth quarter will include a full quarter of activity for Delve, compared to two months of activity during the quarter ended September 30, 2010. We expect that share-based compensation expense will decrease in 2010.

**Sales and Marketing**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009 (in thousands)	Increase (Decrease)	Percent Change	2010	2009 (in thousands)	Increase (Decrease)	Percent Change
Sales and marketing	\$ 12,724	\$ 8,060	\$ 4,664	58%	\$ 33,429	\$ 23,915	\$ 9,514	40%

Sales and marketing expenses consist primarily of payroll and related costs, share-based compensation and commissions for personnel engaged in marketing, sales and service support functions, professional fees (consultants and recruiting fees), travel and travel-related expenses as well as advertising and promotional expenses.

Sales and marketing expenses increased 58%, or \$4.6 million, to \$12.7 million for the three months ended September 30, 2010, as compared to \$8.1 million for the three months ended September 30, 2009. The increase in sales and marketing expenses for the three months ended September 30, 2010 compared to the three months ended September 30, 2009 was primarily due to an increase in payroll and related employee costs of \$3.3 million, primarily due to increased staffing, which resulted in higher salaries, commissions and bonuses, plus the addition of sales and marketing personnel from our business acquisitions, an increase in marketing expenses of \$0.6 million, an increase in travel and travel-related expenses of \$0.4 million and an increase in other expenses of \$0.3 million. For the nine months ended September 30, 2010, sales and marketing expenses increased 40%, or \$9.5 million, to \$33.4 million, as compared to \$23.9 million for the nine months ended September 30, 2009. The increase in sales and marketing expenses for the nine month period ended September 30, 2010 compared to the nine month period ended September 30, 2009 was due to an increase in payroll and related employee costs of \$6.7 million, primarily due to increased staffing, which resulted in higher salaries, commissions and bonuses, plus the addition of sales and marketing personnel from our business acquisitions, an increase in travel and travel-related expenses of \$0.9 million, an increase in marketing expenses of \$0.9 million, an increase in professional fees for outside services of approximately \$0.5 million, and an increase in other expenses of \$0.4 million. Other expenses include such items as rent and property taxes for our Europe and Asia Pacific sales offices, fees, licenses and non-income taxes, telephone and office supplies.

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Additionally, sales and marketing share-based compensation expense remained constant at \$1.3 million for the three month periods ended September 30, 2010 and 2009, respectively. For the nine month period ended September 30, 2010, share-based compensation increased \$0.1 million to \$3.8 million, compared to \$3.7 million for the nine month period ended September 30, 2009.

**Table of Contents**

Sales and marketing expense was composed of the following (in millions):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Payroll and related employee costs	\$ 8.3	\$ 5.0	\$ 21.5	\$ 14.8
Share-based compensation	1.3	1.3	3.8	3.7
Travel and travel-related expenses	1.0	0.6	2.6	1.7
Professional fees and outside services	0.4	0.4	1.5	1.0
Marketing programs	0.8	0.2	1.5	0.6
Other expenses	0.9	0.6	2.5	2.1
<b>Total sales and marketing</b>	<b>\$ 12.7</b>	<b>\$ 8.1</b>	<b>\$ 33.4</b>	<b>\$ 23.9</b>

We anticipate our sales and marketing expense will increase in 2010 in absolute dollars and slightly increase as a percentage of revenue. The increase is due to expected increases in commissions on higher forecasted sales, an increase in payroll and related costs of sales and marketing personnel and additional expected increases in travel and travel-related expenses. In addition, the fourth quarter will include a full quarter of activity for Delve, compared to two months of activity during the quarter ended September 30, 2010. We expect that share-based compensation expense will slightly increase compared to 2009.

**Research and Development**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009 (in thousands)	Increase (Decrease)	Percent Change	2010	2009 (in thousands)	Increase (Decrease)	Percent Change
Research and development	\$ 4,491	\$ 2,024	\$ 2,467	122%	\$ 10,614	\$ 5,878	\$ 4,736	81%

Research and development expenses consist primarily of payroll and related costs and share-based compensation expense for research and development personnel who design, develop, test and enhance our services, network and software.

Research and development expenses increased 122%, or \$2.5 million, to \$4.5 million for the three months ended September 30, 2010, as compared to \$2.0 million for the three months ended September 30, 2009. For the nine months ended September 30, 2010, research and development expenses increased 81%, or \$4.7 million, to \$10.6 million, as compared to \$5.9 million for the nine months ended September 30, 2009. The increase in research and development expenses in the three and nine month periods ended September 30, 2010 as compared to the three and nine month periods ended September 30, 2009 was primarily due to an increase of \$1.6 million and \$3.2 million respectively, in payroll and related employee costs associated with our hiring of additional network and software engineering personnel and the addition of research and development personnel resulting from our business acquisitions, an increase in professional fees and outside services of \$0.4 million and \$0.8 million, respectively, primarily for consulting and contract labor, an increase in share-based compensation of \$0.2 million and \$0.4 million, respectively, and an increase in other expenses of \$0.3 million and \$0.3 million, respectively. Other expenses include such items as travel and travel related expenses, telephone, training and seminars and office supplies.

Research and development expense was composed of the following (in millions):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Payroll and related employee costs	\$ 2.8	\$ 1.2	\$ 6.5	\$ 3.3
Share-based compensation	0.8	0.6	2.3	1.9
Professional fees and outside services	0.5	0.1	1.3	0.5
Other expenses	0.4	0.1	0.5	0.2
<b>Total research and development</b>	<b>\$ 4.5</b>	<b>\$ 2.0</b>	<b>\$ 10.6</b>	<b>\$ 5.9</b>

We anticipate our research and development expenses will increase in 2010 in absolute dollars and increase as a percentage of revenue due to increased payroll and related costs associated with continued hiring of research and development personnel and contractors, and investments in our core technology and refinements to our other service offerings. In addition, the fourth quarter will

**Table of Contents**

include a full quarter of activity for Delve, compared to two months of activity during the quarter ended September 30, 2010. We expect that share-based compensation expense will increase compared to 2009.

**Depreciation and Amortization (Operating Expenses)**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009	Increase (Decrease)	Percent Change	2010	2009	Increase (Decrease)	Percent Change
	(in thousands)				(in thousands)			
Depreciation & amortization	\$ 2,034	\$ 627	\$ 1,407	224%	\$ 4,404	\$ 1,699	\$ 2,705	159%

Depreciation expense consists of depreciation on equipment and furnishing used by general administrative, sales and marketing and research and development personnel. Amortization expense consists of amortization of intangible assets acquired in business combinations.

Depreciation and amortization expenses increased 224%, or \$1.4 million, to \$2.0 million for the three months ended September 30, 2010, as compared to \$0.6 million for the three months ended September 30, 2009. For the nine months ended September 30, 2010, depreciation and amortization expenses increased 159%, or \$2.7 million, to \$4.4 million, as compared to \$1.7 million for the nine months ended September 30, 2009. The increase in depreciation and amortization expense in the three and nine month periods ended September 30, 2010 as compared to the three and nine month periods ended September 30, 2009 was primarily due to an increase of approximately \$1.3 million and \$2.4 million respectively, in amortization of intangibles acquired in business combinations. For the three and nine months ended September 30, 2010, amortization of intangibles was approximately \$1.4 million and \$2.4 million respectively. Based on our intangible assets at September 30, 2010, we expect amortization of other intangible assets to be approximately \$1.4 million for the remainder of 2010, and \$5.5 million, \$5.2 million, \$4.6 million and \$1.3 million for fiscal years 2011, 2012, 2013 and 2014, respectively.

**Provision for Litigation**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009	Increase (Decrease)	Percent Change	2010	2009	Increase (Decrease)	Percent Change
	(in thousands)				(in thousands)			
Provision for litigation	\$	\$	\$	NA	\$	\$ (65,645)	\$ 65,645	100%

The provision for litigation related to our accrual for potential damages and interest associated with revenue generated from allegedly infringing methods associated with the Akamai litigation. At December 31, 2008, the total accrual was \$65.6 million. Based upon an April 24, 2009 court order setting aside the adverse jury verdict and ruling that we did not infringe Akamai's 703 patent and that we are entitled to judgment as a matter of law, we reversed this provision for litigation of \$65.6 million during the first quarter of 2009 as we no longer believe that payment of any amounts represented by the litigation provision is probable.

**Interest Expense**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009	Increase (Decrease)	Percent Change	2010	2009	Increase (Decrease)	Percent Change
	(in thousands)				(in thousands)			
Interest expense	\$ 6	\$ 11	\$ (5)	(45)%	\$ 13	\$ 33	\$ (20)	(61)%

Interest expense consists of interest paid and the amortization of deferred financing costs.

Interest expense decreased 45%, or \$5,000, to \$6,000 for the three months ended September 30, 2010, as compared to \$11,000 for the three months ended September 30, 2009. For the nine months ended September 30, 2010, interest expense decreased 61%, or \$20,000, to \$13,000, as compared to \$33,000 for the nine months ended September 30, 2009. Interest expense for the three and nine month periods ended September 30, 2010 included interest paid in association with a filing of non-income tax related payments and interest paid on capital leases. The \$11,000 and \$33,000 for the three and nine month periods ended September 30, 2009 represents the amortization of loan fees associated with a then unused line of credit. The line of credit expired on October 31, 2009 and we did not renew it. As of September 30, 2010, with the exception of our

capital leases, we had no outstanding credit facilities.

**Table of Contents****Interest Income**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009	Increase (Decrease)	Percent Change	2010	2009	Increase (Decrease)	Percent Change
	(in thousands)				(in thousands)			
Interest income	\$ 210	\$ 330	\$ (120)	(36)%	\$ 767	\$ 1,050	\$ (283)	(27)%

Interest income includes interest earned on invested cash balances and marketable securities.

Interest income decreased 36%, to \$0.2 million for the three months ended September 30, 2010, as compared to \$0.3 million for the three months ended September 30, 2009. For the nine months ended September 30, 2010, interest income decreased 27%, to \$0.8 million, as compared to \$1.0 million for the nine months ended September 30, 2009. The decrease in interest income for the three and nine month periods ended September 30, 2010 was primarily due to decreased cash balances. We anticipate interest income to decrease as a result of expected lower average cash balances.

**Other Income**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009	Increase (Decrease)	Percent Change	2010	2009	Increase (Decrease)	Percent Change
	(in thousands)				(in thousands)			
Other income (expense)	\$ (120)	\$ 15	\$ (135)	(870)%	\$ (117)	\$ 131	\$ (248)	(189)%

Other income (expense) decreased 870% or \$135,000 to \$(120,000) for the three month period ended September 30, 2010, as compared to \$15,000 for the three months ended September 30, 2009. For the nine months ended September 30, 2010, other income (expense) decreased 189%, or \$248,000, to \$(117,000), as compared to \$131,000 for the nine months ended September 30, 2009. Other income (expense) for the three and nine months ended September 30, 2010 consists primarily of foreign exchange gains (losses) resulting from the re-measurement of certain accounts payable and value added tax receivable/payable denominated in a foreign currency of approximately \$(243,000) and \$(7,000), respectively. These foreign exchange gains (losses) were offset by the effect of exchange rates on monetary balance sheet and income statement items of approximately \$118,000 and \$(71,000), respectively. Additionally, miscellaneous other income/expense for the three and nine months ended September 30, 2010 were \$4,000 and \$(39,000), respectively. Other income/expense for the nine month period ended September 30, 2009 includes a non-income tax related expense of approximately \$64,000.

**Income Tax Expense (Benefit)**

	Three months ended September 30,				Nine months ended September 30,			
	2010	2009	Increase (Decrease)	Percent Change	2010	2009	Increase (Decrease)	Percent Change
	(in thousands)				(in thousands)			
Income tax expense (benefit)	\$ 287	\$ 61	\$ 226	370%	\$ (4,570)	\$ 552	\$ 5,122	928%

Based upon our estimated annual effective tax rate, our estimated tax expense for the nine months ended September 30, 2010 consisted of federal, foreign and state expense (benefit) for income taxes. Our income tax benefit on our loss before taxes of \$18.6 million was different than our statutory income tax rate due primarily to our providing for a valuation allowance on tax assets, and recording of discrete items and foreign tax for the quarter. The effective income tax rate is based primarily upon forecasted income or loss for the year, the composition of the income or loss in different countries, and adjustments, if any, for the potential tax consequences, benefits or resolutions for tax audits. In calculating our effective income tax rate for 2010, no benefit is provided for temporary differences that increase deferred tax assets.

For the nine months ended September 30, 2010, our benefit for income taxes was \$4.6 million, which included \$1.1 million for income taxes related primarily to our foreign operations, \$0.1 million for state tax expense and a tax benefit of \$5.8 million related to the release of valuation



## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

allowance as a discrete item as a result of deferred tax liabilities assumed in the acquisition of EyeWonder. During the nine months ended September 30, 2010, we performed an assessment of the recoverability of deferred tax assets. As a result of the acquisition of EyeWonder, \$5.8 million of net deferred tax liabilities were recorded resulting from the temporary differences generated by the differences between the fair value of assets and liabilities acquired (mainly intangible assets such as existing technologies) and their corresponding tax bases. We determined that \$5.8 million of our pre-acquisition deferred tax assets that had a full valuation allowance are now more-likely-than-not to be realized as a result of the acquisition by offsetting such deferred tax assets against the \$5.8 million net deferred tax liabilities recorded as of the acquisition date. Therefore, we recorded a tax benefit of \$5.8 million related to the partial release of the related valuation allowance. For the remaining balance of deferred tax

## **Table of Contents**

assets, there was sufficient negative evidence as a result of our cumulative losses to conclude that it was more-likely-than-not that our deferred tax assets would not be realized and we accordingly maintained the remaining valuation allowance. Related to the Chors and Kiptronic acquisitions, we also have certain taxable temporary differences related to intangible assets that cannot be offset by existing deductible temporary differences resulting in a deferred tax liability of approximately \$602,000.

In 2009, approximately \$3.2 million of stock-based compensation expense was not deductible for tax purposes, as certain executives and other employees made tax elections which established tax bases in these awards granted at lower than the fair value recognized within the financial statements. Future non-tax deductible expenses related to these equity awards is expected to be approximately \$0.6 million for 2010, based upon the unvested portion of the equity awards outstanding at December 31, 2009, and the anticipated vesting at that time.

## **Liquidity and Capital Resources**

To date, we have financed our operations primarily through the following transactions:

private sales of common and preferred stock and subordinated notes;

an initial public offering of our common stock in June 2007;

borrowing on credit facilities; and

cash generated by operations.

As of September 30, 2010, our cash, cash equivalents and marketable securities classified as current totaled \$70.7 million.

## ***Operating Activities***

Net cash provided by operating activities improved by \$13.2 million, with net cash provided by operating activities equaling \$7.6 million for the nine months ended September 30, 2010, compared to net cash used in operating activities of \$5.6 million for the nine months ended September 30, 2009. The change to net cash provided by operating activities for the nine-month period ended September 30, 2010 compared to the same period in the prior year was primarily due to changes in operating assets and liabilities. Cash used due to changes in operating assets and liabilities was \$8.6 million in the nine months ended September 30, 2010 compared to \$22.0 million in the nine months ended September 30, 2009, a decrease in usage of \$13.4 million. The change relates primarily to greater cash usage during the nine months ended September 30, 2009 related primarily to (1) increases in prepaid expenses and other current and long-term assets associated with advanced payments for backbone services with a telecommunications provider; (2) a decrease in accounts payable related to the timing of payments; and (3) a decrease in other current liabilities primarily due to the payment of certain accrued legal fees and cost of sales accruals; and (4) a decrease in deferred revenue resulting from revenue recognition, offset by cash generated from a decrease in accounts receivable due to collection efforts during this period.

We expect that cash provided by operating activities may not be sufficient to cover new purchases of property and equipment during 2010 and litigation expenses associated with patent litigation. The timing and amount of future working capital changes, requirement to secure potential infringement damages and our ability to manage our days sales outstanding will also affect the future amount of cash used in or provided by operating activities.

## ***Investing Activities***

Cash used in investing activities was \$45.8 million for the nine months ended September 30, 2010, compared to cash used in investing activities of \$30.0 million for the nine months ended September 30, 2009. Cash used in investing activities was principally comprised of cash used for the acquisition of businesses, the purchase of short-term marketable securities and capital expenditures primarily for computer equipment associated with the build-out and expansion of our CDN, offset by cash generated from the sale of short-term marketable securities.

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

In January 2010, we acquired chors GmbH or chors, an on-line and direct marketing solutions provider located in Germany. Cash paid, net of cash acquired for the chors acquisition was approximately \$2.0 million.

On April 30, 2010, we acquired EyeWonder, Inc. or EyeWonder. EyeWonder is a provider of interactive digital advertising products and services to advertisers, advertising agencies and publishers. The purchase price included both cash and company stock for the acquisition. Cash paid, net of cash acquired was \$61.9 million.

On July 30, 2010, we acquired Delve Networks, Inc. a privately-held provider of cloud-based video publishing and analytics services located in Seattle, Washington. The transaction was completed with a combination of our common stock and cash. Cash paid, net of cash acquired, was \$2.6 million excluding a potential earn-out payment of \$0.2 million.

**Table of Contents**

We expect to have ongoing capital expenditure requirements as we continue to invest in and expand our CDN. We currently anticipate making aggregate capital expenditures of approximately 16% to 18% of total revenue in 2010.

**Financing Activities**

Cash provided by financing activities relates to proceeds from the exercise of stock options which were \$0.5 million for the nine months ended September 30, 2010, as compared to \$0.2 million for the nine months ended September 30, 2009.

At September 30, 2009, we had an unused line of credit of up to \$5.0 million dollars. The line of credit matured on October 31, 2009 and we did not renew it. At September 30, 2010, with the exception of our capital leases, we had no other debt obligations.

On July 27, 2010, we entered into a lease agreement with a vendor to purchase equipment. Under the terms of the agreement, we financed approximately \$2.3 million, excluding applicable taxes, of equipment for a period of thirty six (36) months. The financing is being accounted for as a capital lease and has been reflected as a non-cash transaction in the condensed consolidated statement of cash flows. The financing agreement is collateralized by the equipment purchased.

We believe that our existing cash and cash equivalents will be sufficient to meet our anticipated cash needs for at least the next 12 months. If the assumptions underlying our business plan regarding future revenue and expenses change, or if unexpected opportunities or needs arise, we may seek to raise additional cash by selling equity or debt securities. If additional funds are raised through the issuance of equity or debt securities, these securities could have rights, preferences and privileges senior to those accruing to holders of common stock, and the terms of such debt could impose restrictions on our operations. The sale of additional equity or convertible debt securities would also result in additional dilution to our stockholders. In the event that additional financing is required from outside sources, we may not be able to raise it on terms acceptable to us or at all. If we are unable to raise additional capital when desired, our business, operating results and financial condition could be harmed.

**Contractual Obligations, Contingent Liabilities and Commercial Commitments**

In the normal course of business, we make certain long-term commitments for operating leases, primarily office facilities, bandwidth and computer rack space. These leases expire on various dates ranging from 2010 to 2019. We expect that the growth of our business will require us to continue to add to and increase our long-term commitments in 2010 and beyond. As a result of our growth strategies, we believe that our liquidity and capital resources requirements will grow.

The following table presents our contractual obligations and commercial commitments, as of September 30, 2010 over the next five years and thereafter (in thousands):

Contractual Obligations as of September 30, 2010	Total	Payments Due by Period			
		Less than 1 year	1-3 years	3-5 years	More than 5 years
Operating Leases					
Bandwidth leases	\$ 19,745	\$ 11,897	\$ 6,712	\$ 1,136	\$
Rack space leases	16,984	6,945	6,269	3,747	23
Real estate leases	16,966	1,928	3,861	4,570	6,607
Total operating leases	53,695	20,770	16,842	9,453	6,630
Capital leases	2,676	977	1,699		
Bank debt					
Interest on bank debt					
Total commitments	\$ 56,371	\$ 21,747	\$ 18,541	\$ 9,453	\$ 6,630

**Off Balance Sheet Arrangements**

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

We do not have, and have never had, any relationships with unconsolidated entities or financial partnerships; such entities are often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

### **Use of Non-GAAP Financial Measures**

To evaluate our business, we consider and use Non-GAAP net income (loss) and Adjusted EBITDA as a supplemental measure of operating performance. These measures include the same adjustments that management takes into account when it reviews and assesses operating performance on a period-to-period basis. We consider Non-GAAP net income (loss) to be an important indicator of overall business performance because it allows us to illustrate the impact of the effects of share-based compensation, litigation expenses, provision for litigation, amortization of intangibles and acquisition related expenses. We define EBITDA as GAAP net

---

**Table of Contents**

income (loss) before interest income, interest expense, other income and expense, provision for income taxes and, depreciation and amortization. We believe that EBITDA provides a useful metric to investors to compare us with other companies within our industry and across industries. We define Adjusted EBITDA as EBITDA adjusted for operational expenses that we do not consider reflective of our ongoing operations. We use Adjusted EBITDA as a supplemental measure to review and assess operating performance. We also believe use of Adjusted EBITDA facilitates investors' use of operating performance comparisons from period to period. In addition, it should be noted that our performance-based executive officer bonus structure is tied closely to our performance as measured in part by certain non-GAAP financial measures.

In our November 5, 2010 earnings press release, as furnished on Form 8-K, we included Non-GAAP net income (loss), EBITDA and Adjusted EBITDA. The terms Non-GAAP net income (loss), EBITDA and Adjusted EBITDA are not defined under United States generally accepted accounting principles, or United States GAAP, and are not measures of operating income, operating performance or liquidity presented in accordance with United States GAAP. Our Non-GAAP net income (loss), EBITDA and Adjusted EBITDA have limitations as analytical tools, and when assessing our operating performance, Non-GAAP net income (loss), EBITDA and Adjusted EBITDA should not be considered in isolation, or as a substitute for net income (loss) or other consolidated income statement data prepared in accordance with United States GAAP. Some of these limitations include, but are not limited to:

EBITDA and Adjusted EBITDA do not reflect our cash expenditures or future requirements for capital expenditures or contractual commitments;

they do not reflect changes in, or cash requirements for, our working capital needs;

they do not reflect the cash requirements necessary for litigation costs;

they do not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, on our debt that we may incur;

they do not reflect income taxes or the cash requirements for any tax payments;

although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will be replaced sometime in the future, and EBITDA and Adjusted EBITDA do not reflect any cash requirements for such replacements;

while share-based compensation is a component of operating expense, the impact on our financial statements compared to other companies can vary significantly due to such factors as the assumed life of the options and the assumed volatility of our common stock; and

other companies may calculate EBITDA and Adjusted EBITDA differently than we do, limiting their usefulness as comparative measures.

We compensate for these limitations by relying primarily on our GAAP results and using Non-GAAP net income (loss) and Adjusted EBITDA only as supplemental support for management's analysis of business performance. Non-GAAP net income (loss), EBITDA and Adjusted EBITDA are calculated as follows for the periods presented.

**Reconciliation of Non-GAAP Financial Measures**

In accordance with the requirements of Regulation G issued by the Securities and Exchange Commission, we are presenting the most directly comparable GAAP financial measures and reconciling the non-GAAP financial metrics to the comparable GAAP measures.

Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Reconciliation of GAAP Net Income (Loss) to Non-GAAP Net Income (Loss)

(In thousands)

(Unaudited)

	Three Months Ended				Nine Months Ended	
	September 30, 2010	June 30, 2010	September 30, 2009	June 30, 2009	September 30, 2010	September 30, 2009
GAAP net (loss) income	\$ (5,954)	\$ (2,265)	\$ (5,220)	\$ (5,298)	\$ (14,004)	\$ 44,617
Provision for potential litigation damages						(65,645)
Share-based compensation	4,554	4,160	4,369	4,281	13,058	13,137
Litigation defense expenses	9	1,726	273	367	2,127	4,585
Acquisition related expenses	345	409			1,358	
Amortization of intangibles	1,354	915	59		2,441	59
Non-GAAP net income (loss)	\$ 308	\$ 4,945	\$ (519)	\$ (650)	\$ 4,980	\$ (3,247)

**Table of Contents****Reconciliation of GAAP Net Income (Loss) to EBITDA to Adjusted EBITDA****(In thousands)****(Unaudited)**

	Three Months Ended				Nine Months Ended	
	September 30, 2010	June 30, 2010	September 30, 2009	June 30, 2009	September 30, 2010	September 30, 2009
GAAP net (loss) income	\$ (5,954)	\$ (2,265)	\$ (5,220)	\$ (5,298)	\$ (14,004)	\$ 44,617
Depreciation and amortization	7,912	6,927	6,645	6,665	20,384	20,398
Interest expense	6	7	11	11	13	33
Interest and other income (expense)	(90)	(283)	(346)	(226)	(650)	(1,181)
Income tax (benefit) expense	287	(5,098)	61	171	(4,570)	552
EBITDA	\$ 2,161	\$ (712)	\$ 1,151	\$ 1,323	\$ 1,173	\$ 64,419
Provision for litigation						(65,645)
Share-based compensation	4,554	4,160	4,369	4,281	13,058	13,137
Litigation defense expenses	9	1,726	273	367	2,127	4,585
Acquisition related expenses	345	409			1,358	
Adjusted EBITDA	\$ 7,069	\$ 5,583	\$ 5,793	\$ 5,971	\$ 17,716	\$ 16,496

**Item 3. Quantitative and Qualitative Disclosures about Market Risk*****Interest Rate Risk***

Our exposure to market risk for changes in interest rates relates primarily to our debt and investment portfolio. In our investment portfolio, we do not use derivative financial instruments. Our investments are primarily with our commercial and investment banks and, by policy, we limit the amount of risk by investing primarily in money market funds, United States Treasury obligations, high-quality corporate and municipal obligations and certificates of deposit. We do not believe that a 10% change in interest rates would have a significant impact on our interest income, operating results or liquidity.

***Foreign Currency Risk***

A significant portion of our customer agreements are denominated in U.S. dollars, and therefore our revenue is not subject to foreign currency risk. Because we have operations in Europe and Asia, however, we may be exposed to fluctuations in foreign exchange rates with respect to certain operating expenses and cash flows. Additionally, we may continue to expand our operations globally and sell to customers in foreign locations, potentially with customer agreements denominated in foreign currencies, which may increase our exposure to foreign exchange fluctuations. At this time, we do not have any foreign currency hedge contracts.

***Inflation Risk***

We do not believe that inflation has had a material effect on our business, financial condition or results of operations. If our costs were to become subject to significant inflationary pressures, we may not be able to fully offset such higher costs through price increases. Our inability or failure to do so could harm our business, financial condition and results of operations.



**Item 4. Controls and Procedures**

***Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures***

We are responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in SEC Rule 13a-15(e) and 15d-15(e). We maintain disclosure controls and procedures, as such term is defined in SEC Rule 13a-15(e) and 15d-15(e), that are designed to ensure that information required to be disclosed in our reports under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As required by SEC Rule 13a-15(b), we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of

## **Table of Contents**

our disclosure controls and procedures as of the end of September 30, 2010. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

### ***Changes in Internal Control over Financial Reporting***

With the exception of the change in controls noted below, no additional changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended September 30, 2010 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

We have implemented a new revenue and invoicing, purchasing, accounts payable and general ledger reporting system. We believe these new reporting systems will further enhance our internal controls over financial reporting. In the future we may make modification and enhancements to the system. There have been no other changes in our internal control over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings**

We are involved in litigation with Akamai Technologies, Inc. and the Massachusetts Institute of Technology relating to a claim of patent infringement. The action was filed in June 2006 in the United States District Court for the District of Massachusetts. The trial date was set for February 2008 with respect to four claims in United States Patent No. 6,108,703 (the '703 patent). In February 2008, a jury returned a verdict in this lawsuit, finding that we infringed four claims of the '703 patent at issue and rejecting our invalidity defenses. The jury awarded an aggregate of approximately \$45.5 million which includes lost profits, reasonable royalties and price erosion damages for the period April 2005 through December 31, 2007. In addition, the jury awarded pre-judgment interest which we estimated to be \$2.6 million at December 31, 2007. We recorded the aggregate \$48.1 million as a provision for litigation as of December 31, 2007. During 2008, we recorded an additional provision of approximately \$17.5 million for potential additional infringement damages and interest. On July 1, 2008, the court denied our Motions for Judgment as a Matter of Law (JMOL), Obviousness, and a New Trial. The court also denied Akamai's Motion for Permanent Injunction as premature and denied its Motions for Summary Judgment regarding our equitable defenses. The court conducted a bench trial in November 2008 regarding our equitable defenses. We also filed a motion for reconsideration of the court's earlier denial of our motion for JMOL. Our motion for reconsideration of JMOL was based largely upon a clarification in the standard for a finding of joint infringement articulated by the Federal Circuit in the case of *Muniauction, Inc. v. Thomson Corp.* (the *Muniauction Case*), released after the court denied our initial motion for JMOL. On April 24, 2009 the court issued its order and memorandum setting aside the adverse jury verdict and ruling that we did not infringe Akamai's '703 patent and that we are entitled to judgment as a matter of law. Based upon the court's April 24, 2009 order we have reversed the \$65.6 million provision for litigation previously recorded for this lawsuit as we no longer believe that payment of any amounts represented by the litigation provision is probable. The court entered final judgment in favor of us. Akamai filed a notice of appeal of the court's decision on May 26, 2009 and filed its appeal brief on September 15, 2009, we filed our reply brief on December 9, 2009 and each party has filed further appeal briefs. The court heard arguments by both parties on June 7, 2010. We cannot assure you that this lawsuit ultimately will be resolved in our favor. We intend to vigorously defend the action should the court rule in Akamai's favor.

We expect that the litigation will continue to be expensive, time consuming and a distraction to our management in operating our business.

In August 2007, we, certain of our officers and directors, and the firms that served as the lead underwriters in our initial public offering were named as defendants in several purported class action lawsuits. These lawsuits have been consolidated into a single lawsuit in United States District Court for the District of Arizona. The consolidated complaint asserts causes of action under Sections 11, 12 and 15 of the Securities Act of 1933, as amended, on behalf of a professed class consisting of all those who were allegedly damaged as a result of acquiring our common stock in our initial public offering (IPO) between June 8, 2007 and August 8, 2007. The complaint seeks compensatory damages and plaintiffs costs and expenses in the litigation. The complaint alleges, among other things, that we omitted and/or misstated certain facts concerning the seasonality of our business and that the loss of revenue with respect to certain customers. On March 17, 2008, we and the individual defendants moved to dismiss all of the plaintiffs' claims, and a hearing was held on this motion on June 16, 2008. On August 8, 2008, the court granted the motion to dismiss, dismissing plaintiffs' claims under Section 12 with prejudice and granting leave to amend the claims under Sections 11 and 15. Plaintiffs chose not to amend the claims under Sections 11 and 15, and on August 29, 2008 the court entered judgment in favor of us. On September 5, 2008, plaintiffs filed a notice of appeal, and appellate briefs were filed by the parties in January and February 2009. We believe that we and the individual defendants have meritorious defenses to the claims made in the complaint and we intend to continue to contest the lawsuit vigorously. We do have in place directors and officers liability insurance and notice of this matter has been given to the insurance carriers. The insurance has reimbursed certain of the expenses incurred by us in defending this action. In November 2009 the parties entered into

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

a Memorandum of Understanding to settle this lawsuit for an amount well within the coverage limits of the primary carrier of our directors and officers liability insurance. We are working to finalize the settlement, which will require court

## Table of Contents

approval. We are not able at this time to estimate the range of a potential loss nor do we believe that a loss is probable. Therefore, we have made no provision for this lawsuit in our financial statements.

In December 2007, Level 3 Communications, LLC (Level 3) filed a lawsuit against us in the United States District Court for the Eastern District of Virginia alleging that we were infringing certain patents Level 3 acquired from Savvis Communications Corp. In addition to monetary relief, including treble damages, interest, fees and costs, the complaint sought an order permanently enjoining us from conducting our business in a manner that infringed the relevant patents. A jury trial was conducted in January 2009, and on January 23, 2009 the jury returned a verdict favorable to us finding that we did not infringe the Level 3 patents. We believe the jury verdict finding Limelight does not infringe the Level 3 patents is correct, and that the claims of infringement asserted against us by Level 3 in the litigation were without merit. The court denied Level 3's subsequent motion for judgment as a matter of law or alternatively for a new trial, and entered a judgment in our favor. Level 3 filed a notice of appeal on July 21, 2009 and filed its appeal brief on October 5, 2009. We filed our reply brief on January 19, 2010. On May 3, 2010 the United States Court of Appeals for the Federal Circuit heard oral argument on this matter, and on May 5, 2010 the court affirmed the District Court judgment in our favor. Level 3 subsequently filed a motion for re-hearing and hearing *en banc* that the Court subsequently denied. In light of the favorable ruling from the Court of Appeals, we do not believe that a loss is probable. Therefore, we have made no provision for this lawsuit in our financial statements.

From time to time, we also may become involved in legal proceedings arising in the ordinary course of our business.

### **Item 1A. Risk Factors**

*Investments in the equity securities of publicly traded companies involve significant risks. Our business, prospects, financial condition or operating results could be materially adversely affected by the risks identified below, as well as other risks not currently known to us or that we currently consider immaterial. The trading price of our common stock could decline due to any of these risks, and you may lose all or part of your investment. In assessing the risks described below, you should also refer to the information contained in this report on Form 10-Q, including our unaudited condensed consolidated financial statements and the related notes, as well as our Annual Report on Form 10-K for the year ended December 31, 2009 and other documents that we file from time to time with the Securities and Exchange Commission.*

#### **Risks Related to Our Business**

*We are a party to several lawsuits, and an adverse outcome in any or all of those lawsuits is possible, which could have a significant, adverse effect on our financial condition and operations. If an injunction were entered against us it could force us to cease providing our CDN services.*

We are a defendant in three significant lawsuits, (see discussion in "Legal Proceedings" in Part II, Item 1 of this quarterly report on Form 10-Q). In each case, we currently have favorable rulings, but we cannot provide any assurance that these favorable rulings won't be overturned or reversed on appeal, or that the ultimate outcome of any of these lawsuits won't be materially adverse to us. The expenses of defending these lawsuits and other lawsuits to which we may become a party, particularly fees paid to our lawyers and expert consultants, have been and will continue to be significant and will continue to adversely affect our operating results during the pendency of the lawsuits. This litigation will also continue to be a distraction to our management in operating our business. We expect that our litigation expenses will continue to be significant on a quarterly basis for the foreseeable future.

In February 2008, a jury returned a verdict in a patent infringement lawsuit filed by Akamai Technologies, Inc., or Akamai, and the Massachusetts Institute of Technology, or MIT, against us, finding that we infringed four claims of the patent at issue and rejecting our invalidity defenses. The jury awarded Akamai an aggregate of approximately \$45.5 million in lost profits, reasonable royalties and price erosion damages, plus pre-judgment interest estimated to be \$2.6 million that we recorded in 2007. During 2008 we recorded an additional provision of approximately \$17.5 million for potential additional infringement damages and interest.

The court conducted a bench trial in November 2008, regarding our equitable defenses; and we filed a motion for reconsideration of the court's earlier denial of our motion for Judgment as a Matter of Law (JMOL). Our motion for JMOL was based largely upon a clarification in the standard for a finding of joint infringement articulated by the Federal Circuit in the case of *Muniauction, Inc. v. Thomson Corp.* (the *Muniauction* Case), released after the court denied our initial motion for JMOL. On April 24, 2009 the court issued its order and memorandum setting aside the adverse jury verdict and ruling that we do not infringe Akamai's 703 patent and that we are entitled to judgment as a matter of law. Based upon the court's April 24, 2009 order we have reversed the provision for litigation relating to this matter as we no longer believe that payment of any amounts represented by the litigation provision is probable. Although the court has entered judgment in our favor and we believe the ruling of the court is correct, Akamai has appealed the judgment, and on June 7, 2010 the United States Court of Appeals for the Federal

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

Circuit heard oral argument on this matter, and a decision is pending. We cannot provide any assurance that the lawsuit ultimately will be resolved in our favor. An adverse ruling could seriously impact our ability to conduct our business and to offer our products and services to our customers. A permanent injunction could prevent us from operating our CDN to deliver certain types of traffic, which could impact the viability of our business. Any adverse ruling, in turn, would harm our revenue, market share, reputation, liquidity and overall financial position.

---

**Table of Contents**

In January 2009, in a patent infringement lawsuit filed against us by Level 3 Communications LLC, or Level 3, a jury returned a verdict finding that we did not infringe any of the claims of the patents at issue in that case. The court denied Level 3's subsequent motion for JMOL or alternatively for a new trial, and entered judgment in our favor. Level 3 has appealed the judgment. On May 3, 2010 the United States Court of Appeals for the Federal Circuit heard oral argument on this matter, and on May 5, 2010 the court affirmed the District Court judgment in our favor.

In August 2007, we, certain of our officers and directors, and the firms that served as the lead underwriters in our initial public offering were named as defendants in several purported class action lawsuits. These lawsuits have been consolidated into a single lawsuit in United States District Court for the District of Arizona. The consolidated complaint asserts causes of action under Sections 11, 12 and 15 of the Securities Act of 1933, as amended, on behalf of a professed class consisting of all those who were allegedly damaged as a result of acquiring our common stock in our initial public offering (IPO) between June 8, 2007 and August 8, 2007. The complaint seeks compensatory damages and plaintiffs costs and expenses in the litigation. The complaint alleges, among other things, that we omitted and/or misstated certain facts concerning the seasonality of our business and the loss of revenue with respect to certain customers. On March 17, 2008, we and the individual defendants moved to dismiss all of the plaintiffs' claims, and a hearing was held on this motion on June 16, 2008. On August 8, 2008, the court granted the motion to dismiss, dismissing plaintiffs' claims under Section 12 with prejudice and granting leave to amend the claims under Sections 11 and 15. Plaintiffs chose not to amend the claims under Sections 11 and 15, and on August 29, 2008 the court entered judgment in favor of us. On September 5, 2008, plaintiffs filed a notice of appeal, and appellate briefs were filed by the parties in January and February 2009. We do have in place directors and officers liability insurance and notice of this matter has been given to the insurance carriers. The insurance has reimbursed certain of the expenses incurred by us in defending this action. In November 2009 the parties entered into a Memorandum of Understanding to settle this lawsuit for an amount well within the coverage limits of the primary carrier of our directors and officers liability insurance. We are working to finalize the settlement, which will require court approval. Although we believe that we and the individual defendants have meritorious defenses to the claims made in the complaint, there can be no assurance at this time that the settlement will be approved by the court, or otherwise completed. If we receive an adverse ruling with respect to the approval of the settlement in this case and we subsequently receive an adverse judgment which exceeds the amount of our directors and officers liability insurance coverage or that insurance is not available to satisfy the judgment, such a ruling could harm our liquidity and overall financial position.

***We may need to defend our intellectual property and processes against patent or copyright infringement claims, which would cause us to incur substantial costs and threaten our ability to do business.***

Companies, organizations or individuals, including our competitors, may hold or obtain patents or other proprietary rights that would prevent, limit or interfere with our ability to make, use or sell our services or develop new services, which could make it more difficult for us to operate our business. From time to time, we may receive inquiries from holders of patents inquiring whether we infringe their proprietary rights. Companies holding Internet-related patents or other intellectual property rights are increasingly bringing suits alleging infringement of such rights or otherwise asserting their rights and seeking licenses. In addition, many of our agreements with customers require us to indemnify such customers for third-party intellectual property infringement claims against them. Pursuant to such agreements, we may be required to defend such customers against certain claims which could cause us to incur additional significant costs. Any litigation or claims, whether or not valid, could result in substantial costs and diversion of resources. See "Legal Proceedings" in Part II, Item 1 of this quarterly report on Form 10-Q. In addition, if we are determined to have infringed upon a third party's intellectual property rights, we may be required to do one or more of the following:

cease selling, incorporating or using products or services that incorporate the challenged intellectual property;

pay substantial damages;

obtain a license from the holder of the infringed intellectual property right, which license may or may not be available on reasonable terms or at all; or

redesign products or services.

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

If we are forced to take any of these actions, our business may be seriously harmed. In the event of a successful claim of infringement against us and our failure or inability to obtain a license to the infringed technology, our business and operating results could be harmed.

***We use certain open-source software the use of which could result in our having to distribute our proprietary software, including our source code, to third parties on unfavorable terms which could materially affect our business.***

Certain of our service offerings use software that is subject to open-source licenses. Open-source code is software that is freely accessible, usable and modifiable. Certain open-source code is governed by license agreements, the terms of which could require users of such open-source code to make any derivative works of such open-source code available to others on unfavorable terms or at no cost. Because we use open-source code, we may be required to take remedial action in order to protect our proprietary software. Such action could include replacing certain source code used in our software, discontinuing certain of our products or taking other actions that could divert resources away from our development efforts.

## **Table of Contents**

In addition, the terms relating to disclosure of derivative works in many open-source licenses are unclear. We periodically review our compliance with the open-source licenses we use and do not believe we will be required to make our proprietary software freely available. However, if a court interprets one or more such open-source licenses in a manner that is unfavorable to us, we could be required to make our software available at no cost.

***We currently face competition from established competitors and may face competition from others in the future.***

We compete in markets that are intensely competitive, rapidly changing and characterized by constantly declining prices and vendors offering a wide range of content delivery solutions. We have experienced and expect to continue to experience increased competition, and particularly aggressive price competition. Many of our current competitors, as well as a number of our potential competitors, have longer operating histories, greater name recognition, broader customer relationships and industry alliances and substantially greater financial, technical and marketing resources than we do. As a consequence of the competitive dynamics in our market we have experienced reductions in our prices, which in turn adversely affect our revenue, gross margin and operating results.

Our primary competitors include content delivery service providers such as Akamai, Level 3 Communications, AT&T, CDNetworks and Internap Network Services Corporation, which acquired VitalStream. Also, as a result of the growth of the content delivery market, a number of companies have recently entered or are currently attempting to enter our market, either directly or indirectly, some of which may become significant competitors in the future. Our largest value-added service, the EyeWonder brand, faces formidable competition in every aspect of our business from other companies that provide solutions and services similar to those offered by us. Currently, the EyeWonder business unit's primary competitors are DoubleClick, Eyeblander, Pointroll, a subsidiary of Gannett, and Atlas. DoubleClick is owned by Google and Atlas is part of the Microsoft Advertising portfolio. DoubleClick and Atlas offer solutions and services similar to those offered by us and compete directly with us. We expect that Google and Microsoft will use their substantial financial and engineering resources to expand the DoubleClick and Atlas businesses and increase their ability to compete with us. We believe that both Google and Microsoft have a greater ability to attract and retain customers due to numerous competitive advantages, including their ability to offer and provide their marketing and advertising customers with a significantly broader range of related solutions and services than us. Google and Microsoft may use their experience and resources to compete with us in a variety of ways, including through acquisitions of competitors or related businesses, and could also use campaign management solutions as a loss leader or provide campaign management solutions without charge or below cost in order to encourage customers to use their other product offerings. The EyeWonder business unit also faces significant competition from rich-media solutions companies such as Unicast (a DG FastChannel company) and UK-based Flashtalking, as well as ad serving companies such as Zedo and CheckM8. In addition, we may experience competition from companies that provide web analytics or web intelligence. Other companies, such as Yahoo!, also are developing campaign management solutions.

Our competitors may be able to respond more quickly than we can to new or emerging technologies and changes in customer requirements. Given the relative ease by which customers typically can switch among providers, differentiated offerings or pricing by competitors could lead to a rapid loss of customers. Some of our current or potential competitors may bundle their offerings with other services, software or hardware in a manner that may discourage content providers from purchasing the services that we offer. In addition, as we expand internationally, we face different market characteristics and competition with local content delivery service providers, many of which are very well positioned within their local markets. Increased competition could result in price reductions and revenue shortfalls, loss of customers and loss of market share, which could harm our business, financial condition and results of operations.

***If we fail to manage future growth effectively, we may not be able to market and sell our services successfully.***

Our future operating results depend to a large extent on our ability to manage expansion and growth successfully. Risks that we face in undertaking this expansion include: training new sales personnel to become productive and generate revenue; forecasting revenue; controlling expenses and investments in anticipation of expanded operations; implementing and enhancing our content delivery network, or CDN, and administrative infrastructure, systems and processes; addressing new markets; and expanding international operations. A failure to manage our growth effectively could materially and adversely affect our ability to market and sell our products and services.

***If we fail to maintain proper and effective internal controls or fail to implement our controls and procedures with respect to acquired or merged operations, our ability to produce accurate financial statements could be impaired, which could adversely affect our operating results, our ability to operate our business and investors' views of us.***

We must ensure that we have adequate internal financial and accounting controls and procedures in place so that we can produce accurate financial statements on a timely basis. We are required to spend considerable effort on establishing and maintaining our internal controls, which



## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

is costly and time-consuming and needs to be re-evaluated frequently.

We have only operated as a public company since June 2007 and we will continue to incur significant legal, accounting and other expenses as we comply with the Sarbanes-Oxley Act of 2002, as well as new rules subsequently implemented by the Securities and Exchange Commission and the Nasdaq Stock Market's Global Market. These rules impose various requirements on public

---

**Table of Contents**

companies, including requiring changes in corporate governance practices, increased reporting of compensation arrangements and other requirements. Our management and other personnel will continue to devote a substantial amount of time to these compliance initiatives. Moreover, these rules and regulations will increase our legal and financial compliance costs and will make some activities more time-consuming and costly. These rules and regulations could also make it more difficult for us to attract and retain qualified persons to serve on our board of directors, our board committees or as executive officers.

Section 404 of the Sarbanes-Oxley Act of 2002 requires that we include in our annual report our assessment of the effectiveness of our internal control over financial reporting and our audited financial statements as of the end of each fiscal year. Furthermore, our independent registered public accounting firm, Ernst & Young LLP, (E&Y), is required to report on whether it believes we maintained, in all material respects, effective internal control over financial reporting as of the end of the year. We successfully completed our assessment and obtained E&Y's attestation as to the effectiveness of our internal control over financial reporting as of December 31, 2009 and 2008, respectively. Our continued compliance with Section 404 will require that we incur substantial expense and expend significant management time on compliance related issues, including our efforts in implementing controls and procedures related to acquired or merged operations. We currently do not have an internal audit group and use an international accounting firm to assist us with our assessment of the effectiveness of our internal controls over financial reporting. In future years, if we fail to timely complete this assessment, or if E&Y cannot timely attest, there may be a loss of public confidence in our internal controls, the market price of our stock could decline and we could be subject to regulatory sanctions or investigations by the Nasdaq Stock Market's Global Market, the Securities and Exchange Commission or other regulatory authorities, which would require additional financial and management resources. In addition, any failure to implement required new or improved controls, or difficulties encountered in their implementation, could harm our operating results or cause us to fail to timely meet our regulatory reporting obligations.

***We may lose customers if they elect to develop content delivery solutions internally.***

Our customers and potential customers may decide to develop their own content delivery solutions rather than outsource these solutions to CDN services providers like us. This is particularly true as our customers increase their operations and begin expending greater resources on delivering their content using third party solutions. If we fail to offer CDN services that are competitive to in-sourced solutions, we may lose additional customers or fail to attract customers that may consider pursuing this in-sourced approach, and our business and financial results would suffer.

***We may lose customers if they are unable to build business models that effectively monetize delivery of their content.***

Some of our customers will not be successful in selling advertising or otherwise monetizing the content we deliver on their behalf and consequently may not be successful in creating a profitable business model. This will result in some of our customers discontinuing their Internet or web-based business operations and discontinuing use of our services and products. Further, weakness and related uncertainty in the global financial markets and economy which has included, among other things, significant reductions in available capital and liquidity from banks and other providers of credit, substantial reductions and/or fluctuations in equity and currency values worldwide and concerns that the worldwide economy may be in a prolonged recessionary period may materially adversely impact our customers' access to capital or willingness to spend capital on our services or in some cases, ultimately cause the customer to file for protection from creditors under applicable insolvency or bankruptcy laws or simply go out of business. This uncertainty may also impact our customers' levels of cash liquidity, which could affect their ability or willingness to timely pay for services that they will order or have already ordered from us. From time to time we discontinue service to customers for non-payment of services. We expect further customers may discontinue operations or not be willing or able to pay for services that they have ordered from us. Further loss of customers may adversely affect our financial results.

***Rapidly evolving technologies or new business models could cause demand for our CDN services to decline or could cause these services to become obsolete.***

Customers or third parties may develop technological or business model innovations that address content delivery requirements in a manner that is, or is perceived to be, equivalent or superior to our CDN services. If competitors introduce new products or services that compete with or surpass the quality or the price/performance of our services, we may be unable to renew our agreements with existing customers or attract new customers at the prices and levels that allow us to generate attractive rates of return on our investment. For example, one or more third parties might develop improvements to current peer-to-peer technology, which is a technology that relies upon the computing power and bandwidth of its participants, such that this technological approach is better able to deliver content in a way that is competitive to our CDN services, or even makes CDN services obsolete. We may not anticipate such developments and may be unable to adequately compete with these potential solutions. In addition, our customers' business models may change in ways that we do not anticipate and these changes could reduce or eliminate our customers' needs for CDN services. If this occurred, we could lose customers or potential customers, and our business and financial results would suffer. As a result of these or similar potential developments, in the future it is possible that competitive dynamics in our market may require us to reduce our prices, which could harm our revenue, gross margin and operating results.



**Table of Contents**

*If we are unable to sell our services at acceptable prices relative to our costs, our revenue and gross margins will decrease, and our business and financial results will suffer.*

Prices for content delivery services have fallen in recent years and are likely to fall further in the future. We have invested significant amounts in purchasing capital equipment to increase the capacity of our content delivery services. For example, in 2007, 2008 and 2009 we invested \$22.3 million, \$17.4 million and \$20.4 million, respectively, in capital expenditures primarily for computer equipment associated with the build-out and expansion of our CDN. For the nine month period ended September 30, 2010, we invested \$25.4 million. Our investments in our infrastructure are based upon our assumptions regarding future demand and also prices that we will be able to charge for our services. These assumptions may prove to be wrong. If the price that we are able to charge customers to deliver their content falls to a greater extent than we anticipate, if we over-estimate future demand for our services or if our costs to deliver our services do not fall commensurate with any future price declines, we may not be able to achieve acceptable rates of return on our infrastructure investments and our gross profit and results of operations may suffer dramatically.

During 2010, as we further expand our CDN and begin to refresh our network equipment, we expect our capital expenditures to be approximately 16% to 18% of total revenue. As a consequence, we are dependent on significant future growth in demand for our services to provide the necessary gross profit to pay these additional expenses. If we fail to generate significant additional demand for our services, our results of operations will suffer and we may fail to achieve planned or expected financial results. There are numerous factors that could, alone or in combination with other factors, impede our ability to increase revenue, moderate expenses or maintain gross margins, including:

failure to increase sales of our core services;

increases in electricity, bandwidth and rack space costs or other operating expenses, and failure to achieve decreases in these costs and expenses relative to decreases in the prices we can charge for our services and products;

inability to maintain our prices relative to our costs;

failure of our current and planned services and software to operate as expected;

loss of any significant customers or loss of existing customers at a rate greater than our increase in new customers or our sales to existing customers;

failure to increase sales of our services to current customers as a result of their ability to reduce their monthly usage of our services to their minimum monthly contractual commitment;

failure of a significant number of customers to pay our fees on a timely basis or at all or failure to continue to purchase our services in accordance with their contractual commitments; and

inability to attract high quality customers to purchase and implement our current and planned services.

*If we are unable to develop new services and enhancements to existing services or fail to predict and respond to emerging technological trends and customers' changing needs, our operating results may suffer.*

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

The market for our CDN and value-added services is characterized by rapidly changing technology, evolving industry standards and new product and service introductions. Our operating results depend on our ability to predict user preferences or industry changes, and modify our solutions and services on a timely basis or develop and introduce new services into existing and emerging markets. The process of developing new technologies is complex and uncertain. We must commit significant resources to developing new services or enhancements to our existing services before knowing whether our investments will result in services the market will accept. Furthermore, we may not execute successfully our technology initiatives because of errors in planning or timing, technical hurdles that we fail to overcome in a timely fashion, misunderstandings about market demand or a lack of appropriate resources. As prices for CDN continue to fall, we will increasingly rely on new product offerings and other value-added services to maintain or increase our gross margins. Failures in execution or market acceptance of new services we introduce could result in competitors providing those solutions before we do, which could lead to loss of market share, revenue and earnings.

*Advertisers may not find Internet advertising effective and may reduce their allocations of advertisement spending on Internet campaigns.*

Most large advertisers have fixed advertising budgets, a very small portion of which is allocated to Internet advertising. The future success of our EyeWonder business depends highly on an increase in the use of the Internet, the commitment of advertisers and advertising agencies to the Internet as an advertising and marketing medium, the advertisers' implementation of advertising campaigns, and the willingness of current or potential customers to outsource their Internet advertising and marketing needs. If the market for Internet advertising or marketing deteriorates, or develops more slowly than we expect, our business could suffer. The market for Internet advertising and marketing is relatively new and rapidly evolving, and we expect that large advertisers will continue to focus most of their advertising efforts on traditional media. Advertisers, including current and potential customers, may also find Internet advertising or marketing to be less effective than traditional media advertising or marketing methods for promoting their products and services, and therefore may decrease the portion of their budget allocated to Internet advertising or may shift their

---

## **Table of Contents**

advertising away from the Internet. Even if Internet advertising increases in the aggregate, if display advertising does not increase, the market for our products and services may not continue to be viable and our revenues may decrease. If we fail to convince these companies to spend a portion of their advertising budgets with us to advertise online, or if our existing advertisers reduce the amount they spend on its services, our business, financial condition or results of operations could be materially adversely affected.

***Our EyeWonder business may be adversely affected by cyclicalities or an extended downturn in the United States or worldwide economy in or related to the industries we serve.***

Revenues for our EyeWonder business unit are generated primarily from providing online campaign management solutions and services to advertising agencies and advertisers across digital media channels and a variety of formats. Demand for these services tends to be tied to economic cycles, reflecting overall economic conditions as well as budgeting and buying patterns. Following the recent negative developments in the world economy, several agency and analyst organizations now predict that the growth in online advertising will be slower than previously expected. We cannot provide assurance that advertising budgets and expenditures by advertising agencies and advertisers will not decline in any given period or that advertising spending will not be diverted to more traditional media or other online marketing products and services, which would lead to a decline in the demand for our campaign management solutions and services. A decline in the economic prospects of advertisers or the economy in general could alter current or prospective customers' spending priorities. As a result, our revenues may not increase or may decline significantly in any given period.

***Consolidation of Internet advertising networks, web portals, Internet search engine sites and web publishers may impair our ability to serve advertisements and to collect campaign data, and could lead to a loss of significant customers.***

The growing trend of consolidation of Internet advertising networks, web portals, Internet search engine sites and web publishers, and increasing industry presence of a small number of large companies, such as Google and Microsoft, could harm our business. We currently are able to serve, track and manage advertisements for our customers in a variety of networks and websites. Concentration of advertising networks or any disruption in our relationship with our publishers could substantially impair our ability to serve advertisements if networks or websites decide not to permit us to serve, track or manage advertisements on their websites, if publishers develop ad placement systems that are not compatible with our systems, or if they use their market power to force their customers to use certain vendors on their networks or websites. These networks or websites also could prohibit or limit our aggregation of advertising campaign data if they use technology that is not compatible with our technology. In addition, concentration of desirable advertising space in a small number of networks and websites could result in pricing pressures and diminish the value of our advertising campaign data, as the value of this data depends to some degree on the continuous aggregation of data from advertising campaigns on a variety of different advertising networks and websites. Additionally, major networks and publishers can terminate our ability to serve advertisements on their properties on short notice. If we are no longer able to serve, track and manage advertisements on a variety of networks and websites, our offerings will be significantly impacted.

***Our EyeWonder business depends on a strong brand reputation, and if we are not able to maintain and enhance our brand, our business will suffer.***

We believe that maintaining and enhancing the EyeWonder brand is critical to expanding our base of customers and maintaining brand loyalty among customers, particularly in North America where brand perception can impact the competitive position in other markets worldwide, and that the importance of brand recognition will increase due to the growing number of competitors providing similar services and solutions. Maintaining and enhancing our brand may require us to make substantial investments in research and development and in the marketing of our solutions and services and these investments may not be successful. If we fail to promote and maintain the EyeWonder brand, or if we incur excessive expenses in this effort, our business and results of operations could be adversely impacted. We anticipate that, as our market becomes increasingly competitive, maintaining and enhancing our brand may become increasingly difficult and expensive. Maintaining and enhancing our brand will depend largely on our ability to be a technology leader and to continue to provide high quality solutions and services, which we may not do successfully.

***New advertisement blocking technologies could limit or block the delivery or display of advertisements by our service offerings, which could undermine the viability of our business.***

Advertisement blocking technologies, such as filter software programs, that can limit or block the delivery or display of advertisements delivered through our service offerings are currently available for Internet users and are continuing to be developed. If these technologies become widespread, the commercial viability of the current Internet advertisement model may be undermined. As a result, ad-blocking technology could, in the future, have a material adverse affect on our business, financial condition and results of operations.

*More individuals are using non-personal computer devices to access the Internet, and the solutions developed for these devices may not be widely deployed.*

---

**Table of Contents**

The number of people who access the Internet through devices other than personal computers (PCs), including mobile devices, game consoles and television set-top devices, has increased dramatically in the past few years. The lower resolution, functionality and memory associated with alternative devices make the use of our service offerings through these devices more difficult and potentially less effective. If we are unable to deliver our service offerings to a substantial number of alternative device users or if we are slow to develop services and technologies that are more compatible with non-PC Internet-enabled devices, we will fail to capture a significant share of an increasingly important portion of the market. Such a failure could limit our ability to compete effectively in an industry that is rapidly growing and changing.

***Our EyeWonder business may be adversely affected by malicious third-party software applications that interfere with the function of our technology.***

Our EyeWonder business may be adversely affected by malicious software applications that make changes to Internet users' computers and interfere with our technology. These applications may attempt to change the users' experience in using our services, including altering or replacing advertisements delivered by our platform, changing configurations of our user interface, or otherwise interfering with our ability to deliver advertisements to users' devices. The interference may occur without disclosure to or consent from users, resulting in a negative experience that users may associate with our services. If our efforts to combat these malicious software applications are unsuccessful, our reputation may be harmed and the communications with certain users on behalf of our customers could be impaired. This could result in a decline in usage of our services and corresponding revenues, which would have a material adverse effect on our business, financial condition and results of operations.

***If we fail to detect click-through fraud or other invalid clicks, we could lose the confidence of our advertisers, thereby causing our business to suffer.***

We are exposed to the risk of fraudulent clicks and other invalid clicks on advertisements delivered by us from a variety of potential sources. Invalid clicks are clicks that we have determined are not intended by the user to link to the underlying content, such as inadvertent clicks on the same ad twice and clicks resulting from click fraud. Click fraud occurs when a user intentionally clicks on an ad displayed on a web site for a reason other than to view the underlying content. These types of fraudulent activities could harm our business and brand. If fraudulent clicks are not detected, the data that our solutions provide to customers may be less reliable and the affected advertisers may lose confidence in our solutions to deliver a return on their investment. If advertisers become dissatisfied with our solutions, they may choose to do business with our competitors or reduce their Internet advertising spending.

***We depend on a limited number of customers for a substantial portion of our revenue in any fiscal period, and the loss of, or a significant shortfall in demand from these customers could significantly harm our results of operations.***

During any given fiscal period, a relatively small number of customers typically account for a significant percentage of our revenue. For example, in 2009, sales to our top 10 customers, in terms of revenue, accounted for approximately 36% of our total revenue. For the nine month period ended September 30, 2010, sales to our top ten customers, in terms of revenue, accounted for approximately 30% of our total revenue. During 2009 one of these top 10 customers, Microsoft, represented approximately 14% of our total revenue for that period. For the nine month period ended September 30, 2010, we had no customer who represented more than 10% of our total revenue. Microsoft, and other large customers, may not continue to be as significant going forward as they have been in the past. During 2011 we anticipate that our revenue from Microsoft will decline from that earned in 2010 and as a percent of our total revenue. In the past, the customers that comprised our top 10 customers have continually changed, and we also have experienced significant fluctuations in our individual customers' usage of our services. As a consequence, we may not be able to adjust our expenses in the short term to address the unanticipated loss of a large customer during any particular period. As such, we may experience significant, unanticipated fluctuations in our operating results which may cause us to not meet our expectations or those of stock market analysts, which could cause our stock price to decline.

***If we are unable to attract new customers or to retain our existing customers, our revenue could be lower than expected and our operating results may suffer.***

In addition to adding new customers, to increase our revenue, we must sell additional services to existing customers and encourage existing customers to increase their usage levels. If our existing and prospective customers do not perceive our services to be of sufficiently high value and quality, we may not be able to retain our current customers or attract new customers. We sell our services pursuant to service agreements that generally include some form of financial minimum commitment. Our customers have no obligation to renew their contracts for our services after the expiration of their initial commitment, and these service agreements may not be renewed at the same or higher level of service, if at all. Moreover, under some circumstances, some of our customers have the right to cancel their service agreements prior to the expiration of the



## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

terms of their agreements. This fact, in addition to the changing competitive landscape in our market, means that we cannot accurately predict future customer renewal rates or usage rates. Our customers' renewal rates may decline or fluctuate as a result of a number of factors, including:

their satisfaction or dissatisfaction with our services;

the prices of our services;

**Table of Contents**

the prices of services offered by our competitors;

discontinuation by our customers of their Internet or web-based content distribution business;

mergers and acquisitions affecting our customer base; and

reductions in our customers' spending levels.

If our customers do not renew their service agreements with us or if they renew on less favorable terms, our revenue may decline and our business will suffer. Similarly, our customer agreements often provide for minimum commitments that are often significantly below our customers' historical usage levels. Consequently, even if we have agreements with our customers to use our services, these customers could significantly curtail their usage without incurring any penalties under our agreements. In this event, our revenue would be lower than expected and our operating results could suffer.

It also is an important component of our growth strategy to market our CDN services to industries, such as enterprise and the government. As an organization, we do not have significant experience in selling our services into these markets. We have only recently begun a number of these initiatives, and our ability to successfully sell our services into these markets to a meaningful extent remains unproven. If we are unsuccessful in such efforts, our business, financial condition and results of operations could suffer.

***Our results of operations may fluctuate in the future. As a result, we may fail to meet or exceed the expectations of securities analysts or investors, which could cause our stock price to decline.***

Our results of operations may fluctuate as a result of a variety of factors, many of which are outside of our control. If our results of operations fall below the expectations of securities analysts or investors, the price of our common stock could decline substantially. In addition to the effects of other risks discussed in this section, fluctuations in our results of operations may be due to a number of factors, including:

our ability to increase sales to existing customers and attract new customers to our CDN and value-added services;

the addition or loss of large customers, or significant variation in their use of our CDN and value-added services;

costs associated with current or future intellectual property lawsuits and other lawsuits;

service outages or security breaches;

the amount and timing of operating costs and capital expenditures related to the maintenance and expansion of our business, operations and infrastructure;

the timing and success of new product and service introductions by us or our competitors;

the occurrence of significant events in a particular period that result in an increase in the use of our CDN and value-added services, such as a major media event or a customer's online release of a new or updated video game;

changes in our pricing policies or those of our competitors;

the timing of recognizing revenue;

limitations of the capacity of our content delivery network and related systems;

the timing of costs related to the development or acquisition of technologies, services or businesses;

general economic, industry and market conditions (such as the fluctuations experienced in the stock and credit markets during the recent deterioration of global economic conditions) and those conditions specific to Internet usage;

limitations on usage imposed by our customers in order to limit their online expenses; and

geopolitical events such as war, threat of war or terrorist actions.

Additionally, the operating results for our EyeWonder business unit have historically fluctuated on a quarterly basis due to the seasonal nature of brand-oriented advertising on the Internet, and we expect this fluctuation to continue. The fourth calendar quarter is typically the strongest, and the first quarter is often the weakest quarter for the EyeWonder business unit. The increase in revenue in the fourth quarter is primarily the result of heavy advertising and online shopping during November and December due to the holidays. The drop in revenues in the first quarter is linked to the drop in online advertising and shopping that occurs at the beginning of each year. We believe that cyclical and seasonality may have a more pronounced effect on our EyeWonder business unit's operating results in the future, as its growth slows. Our EyeWonder business unit's operating expenses are relatively fixed in the near term. As a result, we cannot quickly react to changes in revenue and therefore, changes in revenue could lead to changes in our operating results.

We believe that our revenue and results of operations may vary significantly in the future and that period-to-period comparisons of our operating results may not be meaningful. You should not rely on the results of one period as an indication of future performance.

---

**Table of Contents**

*After being profitable in 2004 and 2005, we were unprofitable in 2006, 2007 and 2008, and would have been unprofitable in 2009, had we not reversed a significant reserve for litigation, primarily due to increased stock-based compensation expense and litigation costs, which could affect our ability to achieve and maintain profitability in the future.*

Our adoption of ASC 718 (formerly FAS 123R) in 2006 substantially increased the amount of share-based compensation expense we record and has had a significant impact on our results of operations. After being profitable in 2004 and 2005, we were unprofitable in 2006, 2007 and 2008 partially due to an increase in our share-based compensation expense which increased from \$0.1 million in 2005 to \$9.2 million in 2006, to \$18.9 million in 2007 to \$18.1 million in 2008. We were profitable in 2009, due to the reversal of a significant reserve for litigation; however our share-based compensation was still significant at \$17.5 million for the year. This significant amount of share-based compensation expense reflects an increase in the level of stock options, restricted stock and restricted stock unit (RSU) grants. Our unrecognized share-based compensation expense totaled \$31.0 million at September 30, 2010, of which we expect to amortize \$4.5 million during the remainder of 2010, \$13.1 million in 2011 and the remainder thereafter based upon the scheduled vesting of the options, restricted stock and RSUs outstanding at that time. The increased share-based compensation expense could adversely affect our ability to achieve and maintain profitability in the future. In 2006, we were sued by Akamai and MIT alleging infringement of certain patents. In December 2007, we were sued by Level 3 Communications alleging infringement of certain patents. We have incurred, and will continue to incur, significant costs associated with litigation. These costs were \$3.1 million, \$7.3 million, \$20.8 million and \$5.4 million, respectively, in 2006, 2007, 2008 and 2009, respectively. For the nine month period ended September 30, 2010, we incurred \$2.1 million in litigation costs. These costs may continue to be significant during 2010.

*We generate our revenue primarily from the sale of CDN services, and the failure of the market for these services to expand as we expect or the reduction in spending on those services by our current or potential customers would seriously harm our business.*

While we offer our customers a number of services associated with our CDN, we generated the majority of our revenue in 2007, 2008, 2009 and the first half of 2010 from charging our customers for the content delivered on their behalf through our CDN. We are subject to an elevated risk of reduced demand for these services. Furthermore, if the market for delivery of rich media content in particular does not continue to grow as we expect or grows more slowly, then we may fail to achieve a return on the significant investment we are making to prepare for this growth. Our success, therefore, depends on the continued and increasing reliance on the Internet for delivery of media content and our ability to cost-effectively deliver these services. Factors that may have a general tendency to limit or reduce the number of users relying on the Internet for media content or the number of providers making this content available online include a general decline in Internet usage, litigation involving our customers and third party restrictions on online content, including copyright restrictions, digital rights management and restrictions in certain geographic regions, as well as a significant increase in the quality or fidelity of offline media content beyond that available online to the point where users prefer the offline experience. The influence of any of these factors may cause our current or potential customers to reduce their spending on CDN services, which would seriously harm our operating results and financial condition.

*Many of our significant current and potential customers are pursuing emerging or unproven business models which, if unsuccessful, could lead to a substantial decline in demand for our CDN services.*

Because the proliferation of broadband Internet connections and the subsequent monetization of content libraries for distribution to Internet users are relatively recent phenomena, many of our customers' business models that center on the delivery of rich media and other content to users remain unproven. For example, social media companies have been among our top recent customers and are pursuing emerging strategies for monetizing the user content and traffic on their web sites. Our customers will not continue to purchase our CDN services if their investment in providing access to the media stored on or deliverable through our CDN does not generate a sufficient return on their investment. A reduction in spending on CDN services by our current or potential customers would seriously harm our operating results and financial condition.

*Our business will be adversely affected if we are unable to protect our intellectual property rights from unauthorized use or infringement by third parties.*

We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. These legal protections afford only limited protection, and we have only one currently issued patent. Monitoring infringement of our intellectual property rights is difficult, and we cannot be certain that the steps we have taken will prevent unauthorized use of our intellectual property rights. We have applied for patent protection in a number of foreign countries, but the laws in these jurisdictions may not protect our proprietary rights as fully as in the United States. Furthermore, we cannot be certain that any pending or future patent applications will be granted, that any future patent will not be challenged, invalidated or circumvented, or that rights granted under any patent that may be issued will provide competitive advantages to us.



---

**Table of Contents**

***Any unplanned interruption in the functioning of our network or services or attacks on our internal information technology systems could lead to significant costs and disruptions that could reduce our revenue and harm our business, financial results and reputation.***

Our business is dependent on providing our customers with fast, efficient and reliable distribution of application and content delivery services over the Internet. Many of our customers depend primarily or exclusively on our services to operate their businesses. Consequently, any disruption of our services could have a material impact on our customers' businesses. Our network or services could be disrupted by numerous events, including natural disasters, failure or refusal of our third party network providers to provide the necessary capacity, failure of our software or CDN delivery infrastructure and power losses. In addition, we deploy our servers in third party co-location facilities, and these third-party co-location providers could experience system outages or other disruptions that could constrain our ability to deliver our services. We may also experience disruptions caused by software viruses or other attacks by unauthorized users.

While we have not experienced any significant, unplanned disruption of our services to date, our CDN may fail in the future. Despite our significant infrastructure investments, we may have insufficient communications and server capacity to address these or other disruptions, which could result in interruptions in our services. Any widespread interruption of the functioning of our CDN and value-added services for any reason would reduce our revenue and could harm our business and financial results. If such a widespread interruption occurred or if we failed to deliver content to users as expected during a high-profile media event, game release or other well-publicized circumstance, our reputation could be damaged severely. Moreover, any disruptions could undermine confidence in our services and cause us to lose customers or make it more difficult to attract new ones, either of which could harm our business and results of operations.

***We may have difficulty scaling and adapting our existing architecture to accommodate increased traffic and technology advances or changing business requirements, which could lead to the loss of customers and cause us to incur unexpected expenses to make network improvements.***

Our CDN services are highly complex and are designed to be deployed in and across numerous large and complex networks. Our network infrastructure has to perform well and be reliable for us to be successful. The greater the user traffic and the greater the complexity of our products and services, the more resources we will need to invest in additional infrastructure and support. Further, as a result of the adverse jury verdict in February 2008 in the Akamai Technologies, Inc. v. Limelight Networks, Inc. lawsuit, which verdict was overturned by the court's April 24, 2009 order granting our motion for judgment as a matter of law, we made significant investment in designing and implementing changes to our CDN architecture in order to implement our CDN services in a manner we believe does not infringe the claims of Akamai's 703 patent as alleged in the February 2008 trial. We have spent and expect to continue to spend substantial amounts on the purchase and lease of equipment and data centers and the upgrade of our technology and network infrastructure to handle increased traffic over our network, implement changes to our CDN architecture and to roll out new products and services. This expansion is expensive and complex and could result in inefficiencies, operational failures or defects in our network and related software. If we do not implement such changes or expand successfully, or if we experience inefficiencies and operational failures, the quality of our products and services and user experience could decline. From time to time, we have needed to correct errors and defects in our software or in other aspects of our CDN. In the future, there may be additional errors and defects that may harm our ability to deliver our services, including errors and defects originating with third party networks or software on which we rely. These occurrences could damage our reputation and lead us to lose current and potential customers. We must continuously upgrade our infrastructure in order to keep pace with our customers' evolving demands. Cost increases or the failure to accommodate increased traffic or these evolving business demands without disruption could harm our operating results and financial condition.

***Our operations are dependent in part upon communications capacity provided by third party telecommunications providers. A material disruption of the communications capacity we have leased could harm our results of operations, reputation and customer relations.***

We lease private line capacity for our backbone from a third party provider, Global Crossing Ltd. Our contracts for private line capacity with Global Crossing generally have terms of three to four years. In January and September 2009, we amended our agreement with Global Crossing to enhance the private line capacity for our backbone. The communications capacity we have leased may become unavailable for a variety of reasons, such as physical interruption, technical difficulties, contractual disputes, or the financial health of our third party provider. As it would be time consuming and expensive to identify and obtain alternative third party connectivity, we are dependent on Global Crossing in the near term. Financial failure of Global Crossing could jeopardize utilization of the service fees pre-paid by us under our agreement with Global Crossing. Additionally, as we grow, we anticipate requiring greater private line capacity than we currently have in place. If we are unable to obtain such capacity on terms commercially acceptable to us or at all, our business and financial results would suffer. We may not be able to deploy on a timely basis enough network capacity to meet the needs of our customer base or effectively manage demand for our services.



---

**Table of Contents**

***Our business depends on continued and unimpeded access to third party controlled end-user access networks.***

Our content delivery services depend on our ability to access certain end-user access networks in order to complete the delivery of rich media and other online content to end-users. Some operators of these networks may take measures, such as the deployment of a variety of filters, that could degrade, disrupt or increase the cost of our or our customers' access to certain of these end-user access networks by restricting or prohibiting the use of their networks to support or facilitate our services, or by charging increased fees to us, our customers or end-users in connection with our services. This or other types of interference could result in a loss of existing customers, increased costs and impairment of our ability to attract new customers, thereby harming our revenue and growth.

In addition, the performance of our infrastructure depends in part on the direct connection of our CDN to a large number of end-user access networks, known as peering, which we achieve through mutually beneficial cooperation with these networks. If, in the future, a significant percentage of these network operators elected to no longer peer with our CDN, the performance of our infrastructure could be diminished, our costs could increase and our business could suffer.

***If our ability to deliver media files in popular proprietary content formats was restricted or became cost-prohibitive, demand for our content delivery services could decline, we could lose customers and our financial results could suffer.***

Our business depends on our ability to deliver media content in all major formats. If our legal right or technical ability to store and deliver content in one or more popular proprietary content formats, such as Adobe Flash or Windows Media, was limited, our ability to serve our customers in these formats would be impaired and the demand for our content delivery services would decline by customers using these formats. Owners of proprietary content formats may be able to block, restrict or impose fees or other costs on our use of such formats, which could lead to additional expenses for us and for our customers, or which could prevent our delivery of this type of content altogether. Such interference could result in a loss of existing customers, increased costs and impairment of our ability to attract new customers, which would harm our revenue, operating results and growth.

***As part of our business strategy, we may acquire businesses or technologies and may have difficulty integrating these operations.***

We may seek to acquire businesses or technologies that are complementary to our business. For example, in May 2009, we acquired substantially all of the assets of Kiptronic Inc., a developer of mobility and monetization solutions for content publishers, in January 2010, we acquired chors GmbH, an on-line and direct marketing solutions provider located in Germany, in April 2010, we acquired EyeWonder, Inc., a provider of interactive digital advertising products and services to advertisers, and in July 2010, we acquired Delve Networks, Inc., a provider of online video solutions to manage, publish, measure and monetize high quality video content on the Internet. Acquisitions involve a number of risks to our business, including the difficulty of integrating the operations and personnel of the acquired companies, the potential disruption of our ongoing business, the potential distraction of management, the possibility that our business culture and the business culture of the acquired companies will not be compatible, the difficulty of incorporating acquired technology and rights into our operations, expenses related to the acquisition and to the integration of the acquired companies, the impairment of relationships with employees and customers as a result of any integration of new personnel, risks related to the businesses of acquired companies that may continue to impact the businesses following the merger and potential unknown liabilities associated with acquired companies. Any inability to integrate operations or personnel in an efficient and timely manner could harm our results of operations.

In order to realize the expected benefits and synergies of our recent merger with EyeWonder, we must meet a number of significant challenges, including:

integrating the management teams, strategies, cultures, technologies and operations of the two businesses;

retaining and assimilating the key personnel of each company;

retaining existing customers; and



## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

implementing and retaining uniform standards, controls, procedures, policies and information systems.

Until the completion of the merger on April 30, 2010, we and EyeWonder had operated independently. It is possible that the integration process could result in the loss of the technical skills and management expertise of key employees, the disruption of each company's ongoing businesses or inconsistencies in standards, controls, procedures and policies due to possible cultural conflicts or differences of opinions on technical decisions and services. A failure to integrate the two organizations successfully could adversely affect our ability to maintain relationships with customers, suppliers and employees or to achieve the anticipated benefits of the merger. Even if we are able to integrate the EyeWonder business operations successfully, this integration may not result in the realization of the full benefits of synergies, cost savings, innovation and operational efficiencies that may be possible from this integration, and these benefits may not be achieved within a reasonable period of time.

**Table of Contents**

We have little prior experience as a company in this complex process of acquiring and integrating businesses. If we are not successful in completing acquisitions that we may pursue in the future, we may be required to reevaluate our business strategy, and we may incur substantial expenses and devote significant management time and resources without a productive result. In addition, future acquisitions will require the use of our available cash or dilutive issuances of securities. Future acquisitions or attempted acquisitions could also harm our ability to achieve profitability. We may also experience significant turnover from the acquired operations or from our current operations as we integrate businesses.

*If we are unable to retain our key employees and hire qualified sales and technical personnel, our ability to compete could be harmed.*

Our future success depends upon the continued services of our executive officers and other key technology, sales, marketing and support personnel who have critical industry experience and relationships that they rely on in implementing our business plan. In particular, we are dependent on the services of our Chief Executive Officer, Jeffrey W. Lunsford and also our Chief Technical Officer, Nathan F. Raciborski. Neither of these officers nor any of our other key employees is bound by an employment agreement for any specific term. There is increasing competition for talented individuals with the specialized knowledge to deliver content delivery services and this competition affects both our ability to retain key employees and hire new ones. The loss of the services of any of our key employees could disrupt our operations, delay the development and introduction of our services, and negatively impact our ability to sell our services.

*We face risks associated with international operations that could harm our business.*

We have operations in numerous foreign countries and may continue to expand our sales and support organizations internationally. As part of our growth strategy, we intend to expand our sales and support organizations internationally, as well as to further expand our international network infrastructure. We have limited experience in providing our services internationally and such expansion could require us to make significant expenditures, including the hiring of local employees, in advance of generating any revenue. As a consequence, we may fail to achieve profitable operations that will compensate our investment in international locations. In addition, expansion into international markets is important to the long-term success of our EyeWonder business, which has only limited experience with operations outside the United States. We are subject to a number of risks associated with international business activities that may increase our costs, lengthen our sales cycle and require significant management attention.

These risks include:

increased expenses associated with sales and marketing, deploying services and maintaining our infrastructure in foreign countries;

competition from local content delivery service providers, many of which are very well positioned within their local markets;

challenges caused by distance, language and cultural differences;

unexpected changes in regulatory requirements preventing us from operating our CDN or resulting in unanticipated costs and delays;

interpretations of laws or regulations that would subject us to regulatory supervision or, in the alternative, require us to exit a country, which could have a negative impact on the quality of our services or our results of operations;

longer accounts receivable payment cycles and difficulties in collecting accounts receivable;

corporate and personal liability for violations of local laws and regulations;

currency exchange rate fluctuations;

potentially adverse tax consequences;

credit risk and higher levels of payment fraud; and

foreign exchange controls that might prevent us from repatriating cash earned in countries outside the United States.

***Internet-related and other laws relating to taxation issues, privacy and consumer protection and liability for content distributed over our network, could harm our business.***

Laws and regulations that apply to communications and commerce conducted over the Internet are becoming more prevalent, both in the United States and internationally, and may impose additional burdens on companies conducting business online or providing Internet-related services such as ours. Increased regulation could negatively affect our business directly, as well as the businesses of our customers, which could reduce their demand for our services. For example, tax authorities abroad may impose taxes on the Internet-related revenue we generate based on where our internationally deployed servers are located. In addition, domestic and international taxation laws are subject to change. Our services, or the businesses of our customers, may become subject to increased

---

**Table of Contents**

taxation, which could harm our financial results either directly or by forcing our customers to scale back their operations and use of our services in order to maintain their operations. In addition, the laws relating to the liability of private network operators for information carried on or disseminated through their networks are unsettled, both in the United States and abroad. Network operators have been sued in the past, sometimes successfully, based on the content of material disseminated through their networks. We may become subject to legal claims such as defamation, invasion of privacy and copyright infringement in connection with content stored on or distributed through our network. In addition, our reputation could suffer as a result of our perceived association with the type of content that some of our customers deliver. If we need to take costly measures to reduce our exposure to these risks, or are required to defend ourselves against such claims, our financial results could be negatively affected.

Several other federal laws also could expose us to liability and impose significant additional costs on us. For example, the Digital Millennium Copyright Act has provisions that limit, but do not eliminate, our liability for the delivery of customer content that infringe copyrights or other rights, so long as we comply with the statutory requirements of the Act. In addition, the Children's Online Privacy Protection Act restricts the ability of online services to collect information from minors and the Protection of Children from Sexual Predators Act of 1998 requires online service providers to report evidence of violations of federal child pornography laws under certain circumstances. Compliance with these laws and regulations is complex and any failure on our part to comply with these regulations may subject us to additional liabilities.

***Privacy concerns could lead to legislative and other limitations on our ability to collect usage data from Internet users, including limitations on our use of cookie or conversion tag technology and user profiling, which is crucial to our ability to provide services to our customers.***

Our ability to conduct targeted advertising campaigns and compile data that we use to formulate campaign strategies for customers depends on the use of cookies and conversion tags to track Internet users and their online behavior, which allows us to measure an advertising campaign's effectiveness and avoid repeatedly delivering the same ad to a particular user's device. A cookie is a small file of information stored on a user's computer that allows us to recognize that user's browser when it serves advertisements. A conversion tag functions similarly to a banner advertisement, except that the conversion tag is not visible. Our conversion tags may be placed on specific pages of clients of customers' or prospective customers' websites. Government authorities inside the United States concerned with the privacy of Internet users have suggested limiting or eliminating the use of cookies, conversion tags or user profiling. Bills aimed at regulating the collection and use of personal data from Internet users are currently pending in U.S. Congress and many state legislatures. Attempts at such regulation may be drafted in such a way as to limit or prohibit the use of technology like cookies and conversion tags, thereby creating restrictions that could reduce our ability to use them. In addition, the Federal Trade Commission and the Department of Commerce have conducted hearings regarding user profiling, the collection of non-personally identifiable information and online privacy.

Our foreign operations may also be adversely affected by regulatory action outside the United States. For example, the European Union has adopted a directive addressing data privacy that limits the collection, disclosure and use of information regarding European Internet users. In addition, the European Union has enacted an electronic communications directive that imposes certain restrictions on the use of cookies and conversion tags and also places restrictions on the sending of unsolicited communications. Each European Union member country was required to enact legislation to comply with the provisions of the electronic communications directive by October 31, 2003 (though not all have done so). Germany has also enacted additional laws limiting the use of user profiling, and other countries, both in and out of the European Union, may impose similar limitations.

Internet users may directly limit or eliminate the placement of cookies on their computers by using third-party software that blocks cookies, or by disabling or restricting the cookie functions of their Internet browser software. Internet browser software upgrades also may result in limitations on the use of cookies or conversion tags. Technologies like the Platform for Privacy Preferences (P3P) Project may limit collection of cookie and conversion tag information. Plaintiffs' attorneys also have organized class action suits against companies related to the use of cookies and several companies, including companies in the Internet advertising industry, have had claims brought against them before the Federal Trade Commission regarding the collection and use of Internet user information. We may be subject to such suits in the future, which could limit or eliminate our ability to collect such information. If our ability to use cookies or conversion tags or engage in other user profiling were substantially restricted due to the foregoing, or for any other reason, we would have to generate and use other technology or methods that allow the gathering of user profile data in order to provide services to customers. This change in technology or methods could require significant reengineering time and resources, and may not be complete in time to avoid negative consequences to our business. In addition, alternative technology or methods might not be available on commercially reasonable terms, if at all. If the use of cookies and conversion tags are prohibited and we are not able to efficiently and cost effectively create new technology, our business, financial condition and results of operations would be materially adversely affected. In addition, any compromise of security that results in the release of Internet users' and/or our customers' data could seriously limit the adoption of our service offerings as well as harm our reputation and brand, expose us to liability and subject us to reporting obligations under various state laws, which could have an adverse effect on our business. The risk that these types of events could seriously harm our business is likely to increase as the amount of data stored for customers on our servers (including personal information) and the number of countries where we operate has been increasing, and we may need to expend significant resources to protect against security breaches, which could have an adverse effect on our business, financial condition or results of operations.



---

**Table of Contents**

*If we are required to seek funding, such funding may not be available on acceptable terms or at all.*

We may need to obtain funding due to a number of factors beyond our control, including a shortfall in revenue, increased expenses, final adverse judgments in litigation matters, increased investment in capital equipment or the acquisition of significant businesses or technologies. We believe that our cash, cash equivalents and marketable securities classified as current plus cash from operations will be sufficient to fund our operations and proposed capital expenditures for at least the next 12 months. However, we may need or desire funding before such time. If we do need to obtain funding, it may not be available on commercially reasonable terms or at all. If we are unable to obtain sufficient funding, our business would be harmed. Even if we were able to find outside funding sources, we might be required to issue securities in a transaction that could be highly dilutive to our investors or we may be required to issue securities with greater rights than the securities we have outstanding today. We might also be required to take other actions that could lessen the value of our common stock, including borrowing money on terms that are not favorable to us. If we are unable to generate or raise capital that is sufficient to fund our operations, we may be required to curtail operations, reduce our capabilities or cease operations in certain jurisdictions or completely.

*Our business requires the continued development of effective business support systems to support our customer growth and related services.*

The growth of our business depends on our ability to continue to develop effective business support systems. This is a complicated undertaking requiring significant resources and expertise. Business support systems are needed for:

implementing customer orders for services;

delivering these services; and

timely billing for these services.

Because our business plan provides for continued growth in the number of customers that we serve and services offered, there is a need to continue to develop our business support systems on a schedule sufficient to meet proposed service rollout dates. The failure to continue to develop effective business support systems could harm our ability to implement our business plans and meet our financial goals and objectives.

*Changes in financial accounting standards or practices may cause adverse, unexpected financial reporting fluctuations and affect our reported results of operations.*

A change in accounting standards or practices can have a significant effect on our operating results and may affect our reporting of transactions completed before the change is effective. New accounting pronouncements and varying interpretations of existing accounting pronouncements have occurred and may occur in the future. Changes to existing rules or the questioning of current practices may adversely affect our reported financial results or the way we conduct our business. For example, our adoption of ASC 718 (formerly FAS 123R) in 2006 has increased the amount of stock-based compensation expense we record. This, in turn, has impacted our results of operations for the periods since this adoption and has made it more difficult to evaluate our recent financial results relative to prior periods.

*We have incurred, and will continue to incur significantly increased costs as a result of operating as a public company, and our management is required to devote substantial time to compliance initiatives.*

As a public company, we have incurred, and will continue to incur, significant accounting and other expenses that we did not incur as a private company. These expenses include increased accounting, legal and other professional fees, insurance premiums, investor relations costs, and costs associated with compensating our independent directors. In addition, the Frank-Dodd Act and the Sarbanes-Oxley Act of 2002, as well as rules subsequently implemented by the Securities and Exchange Commission and the Nasdaq Global Market, imposes additional requirements on public companies, including requiring changes in corporate governance practices. For example, the listing requirements of the Nasdaq Global Market require that we satisfy certain corporate governance requirements relating to independent directors, audit committees, distribution of annual and interim reports, stockholder meetings, stockholder approvals, solicitation of proxies, conflicts of interest, stockholder voting rights and codes of conduct. Our management and other personnel need to devote a substantial amount of time to these compliance initiatives. Moreover, these rules and regulations have increased our legal and financial compliance costs and make some activities more time-consuming

## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

and costly. For example, these rules and regulations make it more difficult and more expensive for us to obtain director and officer liability insurance. These rules and regulations could also make it more difficult for us to identify and retain qualified persons to serve on our board of directors, our board committees or as executive officers.

---

## **Table of Contents**

***Failure to effectively expand our sales and marketing capabilities could harm our ability to increase our customer base and achieve broader market acceptance of our services.***

Increasing our customer base and achieving broader market acceptance of our services will depend to a significant extent on our ability to expand our sales and marketing operations. Historically, we have concentrated our sales force at our headquarters in Tempe, Arizona. However, we are also building a field sales force to augment our sales efforts and to bring our sales personnel closer to our current and potential customers. Developing such a field sales force has been and will continue to be expensive and we have limited knowledge in developing and operating a widely dispersed sales force. As a result, we may not be successful in developing an effective sales force, which could cause our results of operations to suffer.

We believe that there is significant competition for both inside and direct sales personnel with the sales skills and technical knowledge that we require. Our ability to achieve significant growth in revenue in the future will depend, in large part, on our success in recruiting, training and retaining sufficient numbers of inside and direct sales personnel. We have expanded our sales and marketing personnel from a total of 13 at December 31, 2004 to 121 at December 31, 2007, to 140 at December 31, 2009. As of September 30, 2010, we had 225 sales and marketing personnel. New hires require significant training and, in most cases, take a significant period of time before they achieve full productivity. Our recent hires and planned hires may not become as productive as we would like, and we may be unable to hire or retain sufficient numbers of qualified individuals in the future in the markets where we do business. Our business will be seriously harmed if these expansion efforts do not generate a corresponding significant increase in revenue.

***If the accounting estimates we make, and the assumptions on which we rely, in preparing our financial statements prove inaccurate, our actual results may be adversely affected.***

Our financial statements have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments about, among other things, taxes, revenue recognition, share-based compensation costs, contingent obligations and doubtful accounts. These estimates and judgments affect the reported amounts of our assets, liabilities, revenue and expenses, the amounts of charges accrued by us, and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances and at the time they are made. If our estimates or the assumptions underlying them are not correct, we may need to accrue additional charges or reduce the value of assets that could adversely affect our results of operations, investors may lose confidence in our ability to manage our business and our stock price could decline.

### **Risks Related to Ownership of Our Common Stock**

***Our limited operating history makes evaluating our business and future prospects difficult, and may increase the risk of your investment.***

Our Company has only been in existence since 2001. A significant amount of our growth, in terms of employees, operations and revenue, has occurred. For example, our revenue has grown from \$5.0 million in 2003 to \$65.2 million in 2006 to \$131.7 million in 2009. As a consequence, we have a limited operating history which makes it difficult to evaluate our business and our future prospects. We have encountered, and will continue to encounter, risks and difficulties frequently experienced by growing companies in rapidly changing industries, such as the risks described in this report on Form 10-Q. If we do not address these risks successfully, our business will be harmed.

***The trading price of our common stock has been, and is likely to continue to be, volatile.***

The trading prices of our common stock and the securities of technology companies generally have been highly volatile. Factors affecting the trading price of our common stock will include:

variations in our operating results;

announcements of technological innovations, new services or service enhancements, strategic alliances or significant agreements by us or by our competitors;



## Edgar Filing: Limelight Networks, Inc. - Form 10-Q

commencement or resolution of, our involvement in and uncertainties arising from, litigation, particularly our current litigation with Akamai and MIT, Level 3 Communications, and our Securities Litigation matter;

recruitment or departure of key personnel;

changes in the estimates of our operating results or changes in recommendations by any securities analysts that elect to follow our common stock;

developments or disputes concerning our intellectual property or other proprietary rights;

the gain or loss of significant customers;

market conditions in our industry, the industries of our customers and the economy as a whole; and

adoption or modification of regulations, policies, procedures or programs applicable to our business.

## **Table of Contents**

In addition, if the market for technology stocks or the stock market in general experiences loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, operating results or financial condition. The trading price of our common stock might also decline in reaction to events that affect other companies in our industry even if these events do not directly affect us.

***If securities or industry analysts do not publish research or reports about our business or if they issue an adverse or misleading opinion or report, our stock, our stock price and trading volume could decline.***

The trading market for our common stock will be influenced by the research and reports that industry or securities analysts publish about us or our business. If any of the analysts who cover us issue an adverse or misleading opinion regarding our stock, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

***Insiders have substantial control over us and will be able to influence corporate matters.***

As of September 30, 2010, our directors and executive officers and their affiliates beneficially owned, in the aggregate, approximately 49% of our outstanding common stock, including approximately 31% beneficially owned by investment entities affiliated with Goldman, Sachs & Co. These stockholders are able to exercise significant influence over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions, such as a merger or other sale of our company or its assets. This concentration of ownership could limit other stockholders' ability to influence corporate matters and may have the effect of delaying or preventing a third party from acquiring control over us.

***Anti-takeover provisions in our charter documents and Delaware law could discourage, delay or prevent a change in control of our company and may affect the trading price of our common stock.***

We are a Delaware corporation and the anti-takeover provisions of the Delaware General Corporation Law may discourage, delay or prevent a change in control by prohibiting us from engaging in a business combination with an interested stockholder for a period of three years after the person becomes an interested stockholder, even if a change in control would be beneficial to our existing stockholders. In addition, our certificate of incorporation and bylaws may discourage, delay or prevent a change in our management or control over us that stockholders may consider favorable. Our certificate of incorporation and bylaws:

authorize the issuance of blank check preferred stock that could be issued by our board of directors to thwart a takeover attempt;

provide for a classified board of directors, as a result of which the successors to the directors whose terms have expired will be elected to serve from the time of election and qualification until the third annual meeting following their election;

require that directors only be removed from office for cause and only upon a majority stockholder vote;

provide that vacancies on the board of directors, including newly created directorships, may be filled only by a majority vote of directors then in office;

limit who may call special meetings of stockholders;

prohibit stockholder action by written consent, requiring all actions to be taken at a meeting of the stockholders; and

require supermajority stockholder voting to effect certain amendments to our certificate of incorporation and bylaws.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

On July 30, 2010, we issued 335,195 shares of our common stock to certain stockholders of Delve Networks, Inc. (Delve) in connection with and as partial consideration for our acquisition of all of the outstanding capital stock of Delve. The aggregate consideration also consisted of approximately \$2.8 million of cash. The fair value of the common stock issued as consideration was approximately \$1.4 million. The sale of such securities was deemed to be exempt from registration under the Securities Act of 1933, as amended (the Securities Act), in reliance on Rule 506 of Regulation D under the Securities Act. There were no more than 35 purchasers issued securities in the transaction, and each purchaser was an accredited investor, as such term is defined in Rule 501 of Regulation D under the Securities Act, or represented that such purchaser had such knowledge and experience in financial or business matters either alone or together with a qualified representative that such purchaser was capable of evaluating the merits and risks of accepting and owning the securities issued in the transaction.

On June 7, 2007, our registration statement on Form S-1 (No. 333-141516) was declared effective in connection with our initial public offering. The offering closed on June 13, 2007, and, as a result, we received net proceeds of approximately \$203.9 million after underwriters' discounts and commissions of approximately \$15.6 million and additional offering-related costs of approximately \$4.0 million.

**Table of Contents**

In June 2007, we used \$23.8 million of the net proceeds to repay the outstanding balance of our credit facility with Silicon Valley Bank. We expect to use the remaining net proceeds for acquisitions of companies complementary to our core CDN business, capital expenditures, working capital and other general corporate purposes. For the nine month period ended September 30, 2010, we made capital expenditures of \$25.4 million and expect aggregate capital expenditures of approximately 16% to 18% of total revenue in 2010. We may also use a portion of our net proceeds to fund acquisitions of complementary businesses, products or technologies. In July 2010, we acquired Delve Networks, Inc. for which we used approximately \$2.8 million, net of cash acquired and could use an additional \$1.2 million if certain financial targets are achieved. On April 30, 2010 we acquired EyeWonder, Inc. for which we used approximately \$62.0 million in cash and in January 2010 we acquired chors GmbH, for which we used approximately \$2.0 million, net of cash acquired and could use an additional \$0.3 million if specific financial targets are achieved during 2010. Pending the uses described above, we intend to invest the net proceeds in a variety of short-term, interest-bearing, investment grade securities. Depending upon the final outcome of pending litigation a portion of the net proceeds may be used to satisfy a final damages judgment, if any.

**ITEM 3. DEFAULT UPON SENIOR SECURITIES**

Not applicable

**ITEM 4. REMOVED AND RESERVED**

**ITEM 5. OTHER INFORMATION**

Not applicable

**Table of Contents****ITEM 6. EXHIBITS**

<b>Exhibit</b>		<b>Incorporated by Reference</b>				
		<b>Form</b>	<b>File No.</b>	<b>Exhibit</b>	<b>Filing Date</b>	<b>Provided Herewith</b>
<b>Number</b>	<b>Exhibit Description</b>					
3.1	Amended and Restated Certificate of Incorporation of the Registrant, as currently in effect.	S-1	333-141516	3.2	5/21/07	
3.2	Amended and Restated Bylaws of the Registrant, as currently in effect.	S-1	333-141516	3.4	3/22/07	
10.31	Amendment No. 2 to Employment Agreement between the Registrant and Michael M. Gordon dated as of July 8, 2010.	8-K	001-33508	99.1	7/14/10	
10.32	Standard Office Lease between the Registrant and GateWay Tempe LLC dated as of July 20, 2010.					X
31.01	Certification of Principal Executive Officer Pursuant to Securities Exchange Act Rule 13a-14(a).					X
31.02	Certification of Principal Financial Officer Pursuant to Securities Exchange Act Rule 13a-14(a).					X
32.01	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350 and Securities Exchange Act Rule 13a-14(b).*					X
32.02	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350 and Securities Exchange Act Rule 13a-14(b).*					X

\* This certification is not deemed filed for purposes of Section 18 of the Securities Exchange Act, or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that Limelight Networks, Inc. specifically incorporates it by reference.

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

LIMELIGHT NETWORKS, INC.

Date: November 5, 2010

By: /s/ Douglas S. Lindroth  
Douglas S. Lindroth  
Senior Vice President, Chief Financial Officer and Treasurer  
(Principal Financial Officer)

57

**Table of Contents****EXHIBIT INDEX**

Exhibit Number	Exhibit Description	Incorporated by Reference			Filing Date	Provided Herewith
		Form	File No.	Exhibit		
3.1	Amended and Restated Certificate of Incorporation of the Registrant, as currently in effect.	S-1	333-141516	3.2	5/21/07	
3.2	Amended and Restated Bylaws of the Registrant, as currently in effect.	S-1	333-141516	3.4	3/22/07	
10.31	Amendment No. 2 to Employment Agreement between the Registrant and Michael M. Gordon dated as of July 8, 2010.	8-K	001-33508	99.1	7/14/10	
10.32	Standard Office Lease between the Registrant and GateWay Tempe LLC dated as of July 20, 2010.					X
31.01	Certification of Principal Executive Officer Pursuant to Securities Exchange Act Rule 13a-14(a).					X
31.02	Certification of Principal Financial Officer Pursuant to Securities Exchange Act Rule 13a-14(a).					X
32.01	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350 and Securities Exchange Act Rule 13a-14(b).*					X
32.02	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350 and Securities Exchange Act Rule 13a-14(b).*					X

\* This certification is not deemed filed for purposes of Section 18 of the Securities Exchange Act, or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that Limelight Networks, Inc. specifically incorporates it by reference.