SALESFORCE COM INC
Form 10-Q
November 25, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended October 31, 2013

OR

¨ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
Commission File Number: 001-32224

salesforce.com, inc.

(Exact name of registrant as specified in its charter)

Delaware	**94-3320693**
(State or other jurisdiction of	**(IRS Employer**

incorporation or organization)	**Identification No.)**

The Landmark @ One Market, Suite 300

San Francisco, California 94105

(Address of principal executive offices)

Telephone Number (415) 901-7000

(Registrant s telephone number, including area code)

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

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

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

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

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

As of October 31, 2013, there were approximately 603.0 million shares of the Registrant s Common Stock outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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Condensed Consolidated Balance Sheets

(in thousands)

	October 31, 2013 (unaudited)	January 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	$ 651,750	$ 747,245
Short-term marketable securities	51,792	120,376
Accounts receivable, net	604,045	872,634
Deferred commissions	126,054	142,311
Prepaid expenses and other current assets	367,245	133,314
Total current assets	1,800,886	2,015,880
Marketable securities, noncurrent	381,765	890,664
Property and equipment, net	1,205,349	604,669
Deferred commissions, noncurrent	109,273	112,082
Capitalized software, net	505,829	207,323
Goodwill	3,495,021	1,529,378
Other assets, net	599,511	168,960
Total assets	$ 8,097,634	$ 5,528,956
Liabilities, temporary equity and stockholders equity		
Current liabilities:		
Accounts payable, accrued expenses and other liabilities	$ 839,302	$ 597,706
Deferred revenue	1,686,262	1,798,640
Convertible 0.75% senior notes, net	541,125	521,278
Term loan, current	30,000	0
Total current liabilities	3,096,689	2,917,624
Convertible 0.25% senior notes, net	1,041,083	0
Term loan, noncurrent	262,500	0
Deferred revenue, noncurrent	48,357	64,355
Other noncurrent liabilities	702,918	175,732
Total liabilities	5,151,547	3,157,711
Temporary equity	33,731	53,612
Stockholders equity:		
Common stock (1)	603	586
Additional paid-in capital (1)	3,121,481	2,410,892
Accumulated other comprehensive income	16,806	17,137
Accumulated deficit	(226,534)	(110,982)

Total stockholders equity	2,912,356	2,317,633
Total liabilities, temporary equity and stockholders equity	$ 8,097,634	$ 5,528,956

(1) Prior period results have been adjusted to reflect the four-for-one stock split through a stock dividend which occurred in April 2013.

See accompanying Notes.

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Condensed Consolidated Statements of Operations

(in thousands, except per share data)

(unaudited)

	Three Months Ended October 31, 2013	Three Months Ended October 31, 2012	Nine Months Ended October 31, 2013	Nine Months Ended October 31, 2012
Revenues:				
Subscription and support	$ 1,004,476	$ 740,600	$ 2,749,541	$ 2,083,313
Professional services and other	71,558	47,798	176,220	132,201
Total revenues	1,076,034	788,398	2,925,761	2,215,514
Cost of revenues (1)(2):				
Subscription and support	198,809	134,183	513,267	361,446
Professional services and other	69,378	52,065	181,631	138,771
Total cost of revenues	268,187	186,248	694,898	500,217
Gross profit	807,847	602,150	2,230,863	1,715,297
Operating expenses (1)(2):				
Research and development	170,690	114,074	450,708	308,292
Marketing and sales	581,229	428,507	1,528,340	1,178,456
General and administrative	153,859	113,757	434,143	318,452
Total operating expenses	905,778	656,338	2,413,191	1,805,200
Loss from operations	(97,931)	(54,188)	(182,328)	(89,903)
Investment income	1,110	3,887	8,851	15,521
Interest expense	(22,929)	(8,190)	(54,468)	(22,593)
Other expense	(4,291)	(4,360)	(6,843)	(4,776)
Loss before benefit from (provision for) income taxes	(124,041)	(62,851)	(234,788)	(101,751)
Benefit from (provision for) income taxes	(393)	(157,446)	119,236	(147,850)
Net loss	$ (124,434)	$ (220,297)	$ (115,552)	$ (249,601)
Basic net loss per share (3)	$ (0.21)	$ (0.39)	$ (0.19)	$ (0.45)
Diluted net loss per share (3)	$ (0.21)	$ (0.39)	$ (0.19)	$ (0.45)
Shares used in computing basic net loss per share (3)	600,467	568,812	594,346	559,836
Shares used in computing diluted net loss per share (3)	600,467	568,812	594,346	559,836

(1) Amounts include amortization of purchased intangibles from business combinations, as follows:

	Three Months Ended October 31, 2013	Three Months Ended October 31, 2012	Nine Months Ended October 31, 2013	Nine Months Ended October 31, 2012
Cost of revenues	$ 33,844	$ 23,247	$ 77,699	$ 58,363
Marketing and sales	15,211	2,995	22,147	8,829

(2) Amounts include stock-based expenses, as follows:

	Three Months Ended October 31, 2013	Three Months Ended October 31, 2012	Nine Months Ended October 31, 2013	Nine Months Ended October 31, 2012
Cost of revenues	$ 12,119	$ 9,336	$ 32,778	$ 24,453
Research and development	27,935	21,984	78,396	53,740

Marketing and sales	73,296	55,304	189,231	142,072
General and administrative	28,186	18,488	66,336	51,530

(3) Prior period results have been adjusted to reflect the four-for-one stock split through a stock dividend which occurred in April 2013.

See accompanying Notes.

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Condensed Consolidated Statements of Comprehensive Loss

(in thousands)

(unaudited)

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2013	**2012**	**2013**	**2012**
Net loss	$ (124,434)	$ (220,297)	$ (115,552)	$ (249,601)
Other comprehensive income (loss), before tax and net of reclassification adjustments:				
Foreign currency translation and other gains (losses)	5,590	3,134	(1,601)	10,081
Unrealized gains (losses) on investments	(450)	1,252	1,388	1,411
Other comprehensive income (loss), before tax	5,140	4,386	(213)	11,492
Tax effect	427	(467)	(118)	(526)
Other comprehensive income (loss), net of tax	5,567	3,919	(331)	10,966
Comprehensive loss	$ (118,867)	$ (216,378)	$ (115,883)	$ (238,635)

See accompanying Notes.

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Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	Three Months Ended October 31, 2013	Three Months Ended October 31, 2012	Nine Months Ended October 31, 2013	Nine Months Ended October 31, 2012
Operating activities:				
Net loss	$ (124,434)	$ (220,297)	$ (115,552)	$ (249,601)
Adjustments to reconcile net loss to net cash provided by operating activities:				
Depreciation and amortization	114,347	59,960	254,610	159,400
Amortization of debt discount and transaction costs	13,343	6,471	36,207	17,511
Amortization of deferred commissions	48,008	39,070	139,864	111,099
Expenses related to employee stock plans	141,536	105,112	366,741	271,795
Excess tax benefits from employee stock plans	(1,578)	(3,160)	(2,166)	(28,905)
Changes in assets and liabilities, net of business combinations:				
Accounts receivable, net	(4,502)	33,664	332,090	270,802
Deferred commissions	(57,968)	(48,251)	(120,798)	(115,591)
Prepaid expenses, current assets and other assets	23,822	195,312	14,542	140,080
Accounts payable, accrued expenses and other liabilities	40,404	(13,204)	(126,154)	(29,393)
Deferred revenue	(55,119)	(48,762)	(175,153)	(91,873)
Net cash provided by operating activities	137,859	105,915	604,231	455,324
Investing activities:				
Business combinations, net of cash acquired	0	(515,760)	(2,614,732)	(574,751)
Land activity and building improvements	0	0	0	(4,106)
Strategic investments	(9,017)	(1,657)	(17,831)	(5,451)
Purchases of marketable securities	(99,050)	(213,505)	(419,795)	(808,409)
Sales of marketable securities	16,820	82,085	1,022,470	630,317
Maturities of marketable securities	427	41,992	21,031	126,879
Capital expenditures	(72,702)	(51,054)	(229,261)	(125,079)
Net cash used in investing activities	(163,522)	(657,899)	(2,238,118)	(760,600)
Financing activities:				
Proceeds from borrowings on convertible senior notes, net	0	0	1,132,750	0
Proceeds from issuance of warrants	0	0	84,800	0
Purchase of convertible note hedge	0	0	(153,800)	0
Proceeds from term loan, net	0	0	298,500	0
Proceeds from employee stock plans	110,710	76,483	217,429	203,874
Excess tax benefits from employee stock plans	1,578	3,160	2,166	28,905
Principal payments on capital lease obligations	(12,440)	(7,664)	(33,047)	(22,717)
Principal payments on term loan	(7,500)	0	(7,500)	0
Net cash provided by financing activities	92,348	71,979	1,541,298	210,062
Effect of exchange rate changes	5,184	995	(2,906)	9,650

Net increase (decrease) in cash and cash equivalents	71,869	(479,010)	(95,495)	(85,564)
Cash and cash equivalents, beginning of period	579,881	1,000,730	747,245	607,284
Cash and cash equivalents, end of period	$ 651,750	$ 521,720	$ 651,750	$ 521,720
Supplemental cash flow disclosure:				
Cash paid during the period for:				
Interest, net	$ 7,200	$ 641	$ 12,391	$ 4,031
Income taxes, net of tax refunds	$ 6,105	$ 6,514	$ 25,626	$ 51,981
Non-cash financing and investing activities:				
Property and equipment acquired under capital leases	$ 13,857	$ 9,788	$ 487,531	$ 25,585
Fair value of equity awards assumed in business combinations	$ 0	$ 37,428	$ 19,037	$ 37,898

See accompanying Notes.

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Notes to Condensed Consolidated Financial Statements

1. Summary of Business and Significant Accounting Policies

Description of Business

Salesforce.com, inc. (the Company) is a provider of enterprise cloud computing services. The Company is dedicated to helping customers of all sizes and industries worldwide transform themselves into customer companies by empowering them to connect with their customers, partners, employees and products in entirely new ways. The Company provides customers with the solutions they need to build a next generation social front office with social and mobile cloud technologies.

Fiscal Year

The Company s fiscal year ends on January 31. References to fiscal 2014, for example, refer to the fiscal year ending January 31, 2014.

Basis of Presentation

The accompanying condensed consolidated balance sheet as of October 31, 2013 and the condensed consolidated statements of operations, the condensed consolidated statements of comprehensive loss and the condensed consolidated statements of cash flows for the three and nine months ended October 31, 2013 and 2012, respectively, are unaudited. The condensed consolidated balance sheet data as of January 31, 2013 was derived from the audited consolidated financial statements which are included in the Company s Form 10-K for the fiscal year ended January 31, 2013, which was filed with the Securities and Exchange Commission (the SEC) on March 8, 2013. The accompanying statements should be read in conjunction with the audited consolidated financial statements and related notes contained in the Company s fiscal 2013 Form 10-K.

The accompanying condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) for interim financial information. Accordingly, they do not include all of the financial information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of the Company s management, the unaudited condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements in the Form 10-K, and include all adjustments necessary for the fair presentation of the Company s statement of financial position as of October 31, 2013, and its results of operations, including its comprehensive loss, and its cash flows for the three and nine months ended October 31, 2013 and 2012. All adjustments are of a normal recurring nature. The results for the three and nine months ended October 31, 2013 are not necessarily indicative of the results to be expected for any subsequent quarter or for the fiscal year ending January 31, 2014.

On March 20, 2013, the Company s certificate of incorporation was amended to increase the number of authorized shares of common stock from 400.0 million to 1.6 billion in order to provide for a four-for-one stock split of the common stock effected in the form of a stock dividend. The record date for the stock split was April 3, 2013, and the additional shares were distributed on April 17, 2013. Each stockholder of record on the close of business on the record date received three additional shares of common stock for each share held. All share and per share data presented herein reflect the impact of the increase in authorized shares and the stock split, as appropriate.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions in the Company s condensed consolidated financial statements and notes thereto.

Significant estimates and assumptions made by management include the determination of:

- the best estimate of selling price of the deliverables included in multiple-deliverable revenue arrangements, the assessment of recoverability of long-lived assets (property and equipment, goodwill and identified intangibles),

the fair value of assets acquired and liabilities assumed for business combinations,

the recognition, measurement and valuation of current and deferred income taxes,

the recognition and measurement of loss contingencies,

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the fair value of stock awards issued, and

the valuation of strategic investments and the determination of other-than-temporary impairments.
Actual results could differ materially from those estimates.

Principles of Consolidation

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

Segments

The Company operates as one operating segment. Operating segments are defined as components of an enterprise for which separate financial information is evaluated regularly by the chief operating decision maker, who is the chief executive officer, in deciding how to allocate resources and assessing performance. Over the past few years, the Company has completed several acquisitions. These acquisitions have allowed the Company to expand its offerings, presence and reach in various market segments of the enterprise cloud computing market. While the Company has offerings in multiple enterprise cloud computing market segments, the Company s business operates in one operating segment because the Company s chief operating decision maker evaluates the Company s financial information and resources and assesses the performance of these resources on a consolidated basis. Since the Company operates in one operating segment, all required financial segment information can be found in the condensed consolidated financial statements.

Concentrations of Credit Risk and Significant Customers

The Company s financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents, marketable securities and trade accounts receivable. Although the Company deposits its cash with multiple financial institutions, its deposits, at times, may exceed federally insured limits. Collateral is not required for accounts receivable. The Company maintains an allowance for doubtful accounts receivable balances. The allowance is based upon historical loss patterns, the number of days that billings are past due and an evaluation of the potential risk of loss associated with delinquent accounts.

No customer accounted for more than five percent of accounts receivable at October 31, 2013 and January 31, 2013, respectively. No single customer accounted for five percent or more of total revenue during the three and nine months ended October 31, 2013 and 2012.

Geographic Locations

As of October 31, 2013 and January 31, 2013, assets located outside the Americas were 10 percent and 16 percent of total assets, respectively.

Revenues by geographical region are as follows (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2013	**2012**	**2013**	**2012**
Americas	$ 769,400	$ 547,399	$ 2,079,043	$ 1,540,326
Europe	194,932	133,791	531,463	376,694
Asia Pacific	111,702	107,208	315,255	298,494
	$ 1,076,034	$ 788,398	$ 2,925,761	$ 2,215,514

Americas revenue attributed to the United States was approximately 96 percent and 94 percent for the three and nine months ended October 31, 2013 and 2012, respectively.

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Revenue Recognition

The Company derives its revenues from two sources: (1) subscription revenues, which are comprised of subscription fees from customers accessing the Company s enterprise cloud computing services and from customers purchasing additional support beyond the standard support that is included in the basic subscription fees; and (2) related professional services such as process mapping, project management, implementation services and other revenue. Other revenue consists primarily of training fees.

The Company commences revenue recognition when all of the following conditions are satisfied:

- there is persuasive evidence of an arrangement;
- the service has been or is being provided to the customer;
- the collection of the fees is reasonably assured; and
- the amount of fees to be paid by the customer is fixed or determinable.

The Company s subscription service arrangements are non-cancelable and do not contain refund-type provisions.

Subscription and Support Revenues

Subscription and support revenues are recognized ratably over the contract terms beginning on the commencement date of each contract, which is the date the Company s service is made available to customers.

Amounts that have been invoiced are recorded in accounts receivable and in deferred revenue or revenue, depending on whether the revenue recognition criteria have been met.

Professional Services and Other Revenues

The majority of the Company s professional services contracts are on a time and material basis. When these services are not combined with subscription revenues as a single unit of accounting, as discussed below, these revenues are recognized as the services are rendered for time and material contracts, and when the milestones are achieved and accepted by the customer for fixed price contracts. Training revenues are recognized as the services are performed.

Multiple-Deliverable Arrangements

The Company enters into arrangements with multiple-deliverables that generally include multiple subscriptions, premium support and professional services. If the deliverables have standalone value upon delivery, the Company accounts for each deliverable separately. Subscription services have standalone value as such services are often sold separately. In determining whether professional services have standalone value, the Company considers the following factors for each professional services agreement: availability of the services from other vendors, the nature of the professional services, the timing of when the professional services contract was signed in comparison to the subscription service start date and the contractual dependence of the subscription service on the customer s satisfaction with the professional services work. To date, the Company has concluded that all of the professional services included in multiple-deliverable arrangements executed have standalone value.

Multiple-deliverables included in an arrangement are separated into different units of accounting and the arrangement consideration is allocated to the identified separate units based on a relative selling price hierarchy. The Company determines the relative selling price for a deliverable based on its vendor-specific objective evidence of selling price (VSOE), if available, or its best estimate of selling price (BESP), if VSOE is not available. The Company has determined that third-party evidence of selling price (TPE) is not a practical alternative due to differences in its service offerings compared to other parties and the availability of relevant third-party pricing information. The amount of revenue allocated to delivered items is limited by contingent revenue, if any.

For certain professional services, the Company has established VSOE as a consistent number of standalone sales of this deliverable have been priced within a reasonably narrow range. The Company has not established VSOE for its subscription services due to lack of pricing consistency, the introduction of new services and other factors. Accordingly, the Company uses its BESP to determine the relative selling price.

The Company determined BESP by considering its overall pricing objectives and market conditions. Significant pricing practices taken into consideration include the Company s discounting practices, the size and volume of the Company s transactions, the customer demographic, the geographic area where services are sold, price lists, its go-to-market strategy, historical standalone sales and contract prices. The determination of BESP is made through consultation with and approval by the Company s management, taking into consideration the go-to-market strategy. As the Company s go-to-market strategies evolve, the Company may modify its pricing practices in the future, which could result in changes in relative selling prices, including both VSOE and BESP.

Deferred Revenue

The deferred revenue balance does not represent the total contract value of annual or multi-year, non-cancelable subscription agreements. Deferred revenue primarily consists of billings or payments received in advance of revenue recognition from subscription services described above and is recognized as the revenue recognition criteria are met. The Company generally invoices customers in annual or quarterly installments. Deferred revenue is influenced by several factors, including seasonality, the compounding effects of renewals, invoice duration, invoice timing and new business linearity within the quarter.

Deferred revenue that will be recognized during the succeeding twelve month period is recorded as current deferred revenue and the remaining portion is recorded as noncurrent.

Deferred Commissions

Deferred commissions are the incremental costs that are directly associated with non-cancelable subscription contracts with customers and consist of sales commissions paid to the Company s direct sales force.

The commissions are deferred and amortized over the non-cancelable terms of the related customer contracts, which are typically 12 to 36 months. The commission payments are paid in full the month after the customer s service commences. The deferred commission amounts are recoverable through the future revenue streams under the non-cancelable customer contracts. The Company believes this is the preferable method of accounting as the commission charges are so closely related to the revenue from the non-cancelable customer contracts that they should be recorded as an asset and charged to expense over the same period that the subscription revenue is recognized. Amortization of deferred commissions is included in marketing and sales expense in the accompanying condensed consolidated statements of operations.

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Cash and cash equivalents are stated at fair value.

Marketable Securities

Management determines the appropriate classification of marketable securities at the time of purchase and reevaluates such determination at each balance sheet date. Securities are classified as available for sale and are carried at fair value, with the change in unrealized gains and losses, net of tax, reported as a separate component on the condensed consolidated statements of comprehensive loss. Fair value is determined based on quoted market rates when observable or utilizing data points that are observable, such as quoted prices, interest rates and yield curves. Declines in fair value judged to be other-than-temporary on securities available for sale are included as a component of investment income. In order to determine whether a decline in value is other-than-temporary, the Company evaluates, among other factors: the duration and extent to which the fair value has been less than the carrying value and its intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair value. The cost of securities sold is based on the specific-identification method. Interest on securities classified as available for sale is also included as a component of investment income.

Fair Value Measurement

The Company measures its cash equivalents, marketable securities and foreign currency derivative contracts at fair value.

The Company reports its financial and non-financial assets and liabilities that are re-measured and reported at fair value at each reporting period.

The additional disclosures regarding the Company s fair value measurements are included in Note 2.

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Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated on a straight-line basis over the estimated useful lives of those assets as follows:

Computer, equipment and software	3 to 9 years
Furniture and fixtures	5 years
Leasehold improvements	Shorter of the lease term or 10 years
Building improvements	Amortized over the estimated useful lives of the respective assets when they are ready for their intended use.

When assets are retired or otherwise disposed of, the cost and accumulated depreciation and amortization are removed from their respective accounts and any loss on such retirement is reflected in operating expenses.

Capitalized Internal-Use Software Costs

The Company capitalizes costs related to its enterprise cloud computing services and certain projects for internal use incurred during the application development stage. Costs related to preliminary project activities and post implementation activities are expensed as incurred. Internal-use software is amortized on a straight line basis over its estimated useful life. Management evaluates the useful lives of these assets on an annual basis and tests for impairment whenever events or changes in circumstances occur that could impact the recoverability of these assets.

Goodwill, Intangible Assets, Long-Lived Assets and Impairment Assessments

The Company evaluates and tests the recoverability of its goodwill for impairment at least annually during the fourth quarter or more often if and when circumstances indicate that goodwill may not be recoverable.

Intangible assets are amortized over their useful lives. Each period the Company evaluates the estimated remaining useful life of its intangible assets and whether events or changes in circumstances warrant a revision to the remaining period of amortization. The carrying amounts of these assets are periodically reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of these assets may not be recoverable. Recoverability of these assets is measured by comparison of the carrying amount of each asset to the future undiscounted cash flows the asset is expected to generate. If the undiscounted cash flows used in the test for recoverability are less than the carrying amount of these assets then the Company will recognize an impairment charge.

The Company evaluates the recoverability of its long-lived assets for possible impairment whenever events or circumstances indicate that the carrying amount of such assets may not be recoverable. If such review indicates that the carrying amount of long-lived assets is not recoverable, the carrying amount of such assets is reduced to fair value.

Business Combinations

The Company uses its best estimates and assumptions to accurately assign fair value to the tangible and intangible assets acquired and liabilities assumed at the acquisition date. The Company s estimates are inherently uncertain and subject to refinement. During the measurement period, which may be up to one year from the acquisition date, the Company may record adjustments to the fair value of these tangible and intangible assets acquired and liabilities assumed, with the corresponding offset to goodwill. In addition, uncertain tax positions and tax-related valuation allowances are initially established in connection with a business combination as of the acquisition date. The Company continues to collect information and reevaluates these estimates and assumptions quarterly and records any adjustments to the Company s preliminary estimates to goodwill provided that the Company is within the measurement period. Upon the conclusion of the measurement period or final determination of the fair value of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the Company s condensed consolidated statements of operations.

Leases and Asset Retirement Obligations

The Company categorizes leases at their inception as either operating or capital leases. On certain lease agreements, the Company may receive rent holidays and other incentives. The Company recognizes lease costs on a straight-line basis once control of the space is achieved, without regard to deferred payment terms, such as rent holidays that defer the commencement date of required payments. Additionally, incentives received are treated as a reduction of costs over the term of the agreement.

The Company establishes assets and liabilities for the present value of estimated future costs to retire long-lived assets at the termination or expiration of a lease. Such assets are depreciated over the lease period into operating expense, and the recorded liabilities are accreted to the future value of the estimated retirement costs.

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Accounting for Stock-Based Compensation

The Company recognizes stock-based expenses related to stock options and restricted stock awards on a straight-line basis over the requisite service period of the awards, which is generally the vesting term of four years. The Company recognizes stock-based expenses related to shares issued pursuant to its Employee Stock Purchase Plan (ESPP) on a straight-line basis over the offering period, which is 12 months. Stock-based expenses are recognized net of estimated forfeiture activity. The estimated forfeiture rate applied is based on historical forfeiture rates.

The fair value of each stock option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions and fair value per share:

	Three Months Ended October 31,		Nine Months Ended October 31,	
Stock Options	**2013**	**2012**	**2013**	**2012**
Volatility	39%	47%	39-43%	47-51%
Estimated life	3.5 years	3.7 years	3.2 years	3.7 years
Risk-free interest rate	1.03-1.21%	0.47-0.57%	0.48-1.21%	0.43-0.77%
Dividend yield	0	0	0	0
Weighted-average fair value per share of grants	$ 14.52	$ 13.02	$ 11.98	$ 13.13

	Three Months Ended October 31,		Nine Months Ended October 31,	
ESPP	**2013**	**2012**	**2013**	**2012**
Volatility	n/a	n/a	31-32%	42-46%
Estimated life	n/a	n/a	0.75 years	0.75 years
Risk-free interest rate	n/a	n/a	0.07-0.10%	0.12-0.13%
Dividend yield	n/a	n/a	0	0
Weighted-average fair value per share of grants	n/a	n/a	$ 9.69	$ 10.09

There were no stock purchase rights granted under the ESPP in the three months ended October 31, 2013 or 2012 as these stock purchase rights are only granted in June and December.

The Company estimated its future stock price volatility considering both its observed option-implied volatilities and its historical volatility calculations. Management believes this is the best estimate of the expected volatility over the expected life of its stock options.

The estimated life for the stock options was based on an analysis of historical expected life. The estimated life for the ESPP was based on the two purchase periods within each offering period. The risk-free interest rate is based on the rate for a U.S. government security with the same estimated life at the time of the option grant.

Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on temporary differences between the financial statement 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 on deferred tax assets and liabilities of a change in tax laws is recognized in the consolidated statement of operations in the period that includes the enactment date. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts more likely than not expected to be realized.

The Company s tax positions are subject to income tax audits by multiple tax jurisdictions throughout the world. The Company recognizes the tax benefit of an uncertain tax position only if it is more likely than not that the position is sustainable upon examination by the taxing authority, based on the technical merits. The tax benefit recognized is measured as the largest amount of benefit which is greater than 50 percent likely to be realized upon settlement with the taxing authority. The Company recognizes interest accrued and penalties related to unrecognized tax benefits in the income tax provision.

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Foreign Currency Translation

The functional currency of the Company s major foreign subsidiaries is generally the local currency. Adjustments resulting from translating foreign functional currency financial statements into U.S. dollars are recorded as a separate component on the condensed consolidated statements of comprehensive loss. Foreign currency transaction gains and losses are included in net loss for the period. All assets and liabilities denominated in a foreign currency are translated into U.S. dollars at the exchange rate on the balance sheet date. Revenues and expenses are translated at the average exchange rate during the period. Equity transactions are translated using historical exchange rates.

Warranties and Indemnification

The Company s enterprise cloud computing services are typically warranted to perform in a manner consistent with general industry standards that are reasonably applicable and materially in accordance with the Company s online help documentation under normal use and circumstances.

The Company s arrangements generally include certain provisions for indemnifying customers against liabilities if its products or services infringe a third-party s intellectual property rights. To date, the Company has not incurred any material costs as a result of such obligations and has not accrued any liabilities related to such obligations in the accompanying condensed consolidated financial statements.

The Company has also agreed to indemnify its directors and executive officers for costs associated with any fees, expenses, judgments, fines and settlement amounts incurred by any of these persons in any action or proceeding to which any of those persons is, or is threatened to be, made a party by reason of the person s service as a director or officer, including any action by the Company, arising out of that person s services as the Company s director or officer or that person s services provided to any other company or enterprise at the Company s request. The Company maintains director and officer insurance coverage that would generally enable the Company to recover a portion of any future amounts paid. The Company may also be subject to indemnification obligations by law with respect to the actions of its employees under certain circumstances and in certain jurisdictions.

New Accounting Pronouncements

In July 2012, the Financial Accounting Standards Board (the FASB) issued Accounting Standards Update No. 2012-02, *Intangibles Goodwill and Other (Topic 350) Testing Indefinite-Lived Intangible Assets for Impairment* (ASU 2012-02), to allow entities to use a qualitative approach to test indefinite-lived intangible assets for impairment. ASU 2012-02 permits an entity to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying value. If it is concluded that this is the case, it is necessary to perform the currently prescribed quantitative impairment test by comparing the fair value of the indefinite-lived intangible asset with its carrying value. Otherwise, the quantitative impairment test is not required. The Company adopted ASU 2012-02 in fiscal 2014 and does not believe that the adoption will have a material effect on the condensed consolidated financial statements.

In July 2013, the FASB issued Accounting Standards Update No. 2013-11, *Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* (ASU 2013-11), which provides guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss (NOL) carryforward, a similar tax loss, or a tax credit carryforward exists. ASU 2013-11 supports the approach for companies to present an unrecognized tax benefit as a reduction of a deferred tax asset for a NOL or tax credit carryforward whenever the NOL or tax credit carryforward would be available to reduce the additional taxable income or tax due if the tax position is disallowed. This approach requires companies to assess whether to net the unrecognized tax benefit with a deferred tax asset as of the reporting date. The Company plans to adopt ASU 2013-11 in fiscal 2015 and is currently evaluating the impact to its consolidated financial statements.

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2. Investments

Marketable Securities

At October 31, 2013, marketable securities consisted of the following (in thousands):

Investments classified as Marketable Securities	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate notes and obligations	$ 262,897	$ 1,037	$ (161)	$ 263,773
U.S. treasury securities	9,826	17	0	9,843
Mortgage backed obligations	26,555	249	(91)	26,713
Asset backed securities	30,274	31	(57)	30,248
Municipal securities	1,000	0	(7)	993
Foreign government obligations	19,807	84	(6)	19,885
U.S. agency obligations	15,224	10	(3)	15,231
Covered bonds	66,363	508	0	66,871
Total marketable securities	$ 431,946	$ 1,936	$ (325)	$ 433,557

At January 31, 2013, marketable securities consisted of the following (in thousands):

Investments classified as Marketable Securities	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate notes and obligations	$ 685,695	$ 5,113	$ (919)	$ 689,889
U.S. treasury securities	38,864	20	(15)	38,869
Mortgage backed obligations	12,447	278	(2)	12,723
Municipal securities	2,697	1	(32)	2,666
Foreign government obligations	9,572	72	(3)	9,641
Collateralized mortgage obligations	150,794	1,775	(693)	151,876
U.S. agency obligations	105,224	157	(5)	105,376
Total marketable securities	$ 1,005,293	$ 7,416	$ (1,669)	$ 1,011,040

The duration of the investments classified as marketable securities is as follows (in thousands):

	As of	
	October 31, 2013	January 31, 2013
Recorded as follows:		
Short-term (due in one year or less)	$ 51,792	$ 120,376
Long-term (due between one and 3 years)	381,765	890,664
	$ 433,557	$ 1,011,040

As of October 31, 2013, the following marketable securities were in an unrealized loss position (in thousands):

Less than 12 Months	12 Months or Greater	Total

	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate notes and obligations	$ 65,202	$ (159)	$ 1,355	$ (2)	$ 66,557	$ (161)
Mortgage backed obligations	8,725	(58)	3,276	(33)	12,001	(91)
Asset backed securities	16,877	(57)	0	0	16,877	(57)
Municipal securities	993	(7)	0	0	993	(7)
Foreign government obligations	9,494	(6)	0	0	9,494	(6)
U.S. agency obligations	9,726	(3)	0	0	9,726	(3)
	$ 111,017	$ (290)	$ 4,631	$ (35)	$ 115,648	$ (325)

The unrealized loss for each of these fixed rate marketable securities ranged from less than $1,000 to $23,000. The Company does not believe any of the unrealized losses represent an other-than-temporary impairment based on its evaluation of available evidence as of October 31, 2013. The Company expects to receive the full principal and interest on all of these marketable securities.

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Fair Value Measurement

All of the Company s cash equivalents, marketable securities and foreign currency derivative contracts are classified within Level 1 or Level 2 because the Company s cash equivalents, marketable securities and foreign currency derivative contracts are valued using quoted market prices or alternative pricing sources and models utilizing observable market inputs.

The Company uses a three-tier fair value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

Level 1. Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2. Other inputs that are directly or indirectly observable in the marketplace.

Level 3. Unobservable inputs which are supported by little or no market activity.

The following table presents information about the Company s assets and liabilities that are measured at fair value as of October 31, 2013 and indicates the fair value hierarchy of the valuation (in thousands):

Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balances as of October 31, 2013
Cash equivalents (1):				
Time deposits	$ 0	$ 211,574	$ 0	$ 211,574
Money market mutual funds	94,372	0	0	94,372
Marketable securities:				
Corporate notes and obligations	0	263,773	0	263,773
U.S. treasury securities	0	9,843	0	9,843
Mortgage backed obligations	0	26,713	0	26,713
Asset backed securities	0	30,248	0	30,248
Municipal securities	0	993	0	993
Foreign government obligations	0	19,885	0	19,885
U.S. agency obligations	0	15,231	0	15,231
Covered bonds	0	66,871	0	66,871
Foreign currency derivative contracts (2)	0	1,718	0	1,718
Total Assets	$ 94,372	$ 646,849	$ 0	$ 741,221
Liabilities				
Foreign currency derivative contracts (3)	$ 0	$ 282	$ 0	$ 282