RAINING DATA CORP
Form 10QSB
February 12, 2003

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U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended December 31, 2002

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

For the transition period from _____________ to _____________
Commission File number 0-16449

RAINING DATA CORPORATION

(Exact name of registrant as specified in its charter)

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

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

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

Check whether the issuer: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

As of January 31, 2003 there were 17,880,983 shares of registrant's Common Stock, $.10 par value, outstanding.

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

RAINING DATA CORPORATION
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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

RAINING DATA CORPORATION AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

	December 31, 2002	March 31, 2002
	(In thousands)	
ASSETS		
Current Assets		
Cash and Equivalents	$ 2,761	$ 4,500
Trade Accounts Receivable-net	1,821	1,575
Other Current Assets	510	190
Total Current Assets	5,092	6,265
Property, Furniture and Equipment-net	920	910
Intangible Assets-net	4,983	6,933
Goodwill & Acquisition Costs-net	27,834	26,791
Other Assets	194	59
Total Assets	$ 39,023	$ 40,958
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts Payable	$ 130	$ 985
Accrued Liabilities	2,963	4,409
Deferred Revenue	4,296	4,189
Current Portion of Long-Term Debt	326	1,207

	December 31, 2002	March 31, 2002
Total Current Liabilities	7,715	10,790
Long-Term Debt-net of discount and excluding current portion	21,464	18,502
Other Long-Term Liabilities		125
Total Liabilities	29,179	29,417
Commitments and Contingencies		
Stockholders' Equity		
Preferred Stock	300	300
Common Stock	1,788	1,759
Additional Paid-in Capital	95,059	93,829
Deferred Stock-based Compensation	(322)	(523)
Accumulated Other Comprehensive Income	1,002	869
Accumulated Deficit	(87,983)	(84,693)
Total Stockholders' Equity	9,844	11,541
Total Liabilities and Stockholders' Equity	$ 39,023	$ 40,958

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

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RAINING DATA CORPORATION AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2002	**2001**	**2002**	**2001**
	(In thousands, except share and per share data)			
Net Revenues				
Licenses	$ 2,494	$ 2,551	$ 6,866	$ 7,625
Services	2,796	2,390	8,085	6,726
Total Net Revenues	5,290	4,941	14,951	14,351
Costs of Revenues				
Cost of License Revenues	62	107	177	300
Cost of Service Revenues	438	410	1,356	2,010
Total Cost of Revenues	500	517	1,533	2,310

	Three Months Ended December 31,		Nine Months Ended December 31,	
Gross Profit	4,790	4,424	13,418	12,041
Cost of Operations				
Selling and Marketing	1,011	1,111	3,088	4,822
Research and Development	1,551	1,314	4,253	4,055
General and Administrative	1,276	2,051	4,187	5,464
Stock-Based Compensation	89	326	354	939
Amortization of Goodwill and Intangibles	650	3,207	1,950	9,589
Total Operating Expense	4,577	8,009	13,832	24,869
Operating Income (Loss)	213	(3,585)	(414)	(12,828)
Other Expense				
Interest Expense-net	(853)	(1,007)	(2,920)	(2,854)
Other Income (Expense)-net	5	(3)	44	(52)
	(848)	(1,010)	(2,876)	(2,906)
Net Loss	$ (635)	$ (4,595)	$ (3,290)	$ (15,734)
Basic and Diluted				
Net Loss Per Share	$ (0.04)	$ (0.29)	$ (0.19)	$ (0.96)
Weighted Average Number of Common Shares Outstanding	17,880,983	15,720,711	17,767,410	16,375,868
Supplemental Information on Stock Based Compensation				
Departmental Allocation of Costs				
Cost of Service Revenue	$ 3	$ 32	$ 8	$ 97
Selling and Marketing	16	36	49	102
Research and Development	57	175	272	384
General and Administrative	13	83	25	356
Total Stock-based Compensation	$ 89	$ 326	$ 354	$ 939

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

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RAINING DATA CORPORATION AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

NINE MONTHS ENDED DECEMBER 31,

	2002	2001
	(In thousands)	
Cash flows from operating activities:		
Net loss	$ (3,290)	$ (15,734)
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation and amortization of long-lived assets	2,230	10,149
Note discount amortization	1,485	2,796
Amortization of deferred stock-based compensation	354	939
Change in assets and liabilities:		
Trade accounts receivable	(115)	42
Other current and non-current assets	(235)	342
Accounts payable and accrued liabilities	(1,746)	(305)
Deferred revenue	(58)	1,128
Net cash used for operating activities	(1,375)	(643)
Cash flows from investing activities:		
Purchases of property, furniture and equipment	(179)	(93)
Purchase of software	(250)	
Net cash used for investing activities	(429)	(93)
Cash flows from financing activities:		
Proceeds from exercise of stock options	2	79
Repayment of debt	(36)	(194)
Proceeds from issuance of common stock	43	2,319
Net cash provided by financing activities	9	2,204
Effect of exchange rate changes on cash	56	24
Net increase (decrease) in cash and equivalents	(1,739)	1,492
Cash and equivalents at beginning of period	4,500	2,424
Cash and equivalents at end of period	$ 2,761	$ 3,916

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

RAINING DATA CORPORATION AND SUBSIDIARIES

CONDENSED NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2002 (Unaudited)

1. INTERIM FINANCIAL STATEMENTS

The unaudited interim condensed consolidated financial information furnished herein reflects all adjustments, consisting only of normal recurring items, which in the opinion of management are necessary to fairly state the Company's financial position, the results of its operations and its cash flows for the dates and periods presented. Certain information and footnote disclosures, normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been omitted pursuant to SEC rules and regulations; nevertheless, management of the Company believes that the disclosures herein are adequate to make the information presented not misleading. These consolidated financial statements should be read in conjunction with the Company's audited financial statements for the year ended March 31, 2002 contained in the Company's Annual Report on Form 10-KSB/A. The results of operations for the period ended December 31, 2002 are not necessarily indicative of results to be expected for any other interim period or the fiscal year ending March 31, 2003.

2. RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2001, the FASB issued SFAS No. 141, "Business Combinations," ("SFAS No. 141") and SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"). SFAS No. 141 requires that the purchase method of accounting be used for all business combinations initiated after September 30, 2001 and eliminates the pooling-of-interests method. SFAS No. 141 specifies criteria that intangible assets acquired in a business combination must meet to be recognized and reported separately from goodwill. SFAS No. 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142. SFAS No. 142 requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values. In addition, SFAS No. 142 includes provisions upon adoption for the reclassification of certain existing recognized intangibles as goodwill, reclassification of certain intangibles out of previously reported goodwill, reassessment of the useful lives of recognized intangibles and testing for impairment of those intangibles.

The Company adopted certain provisions of SFAS No. 141 as of July 1, 2001 as required for business combinations initiated after July 1, 2001, and the remaining provisions of SFAS No. 141 and SFAS No. 142 became effective for the Company on April 1, 2002. Upon adoption of SFAS No. 142, the Company was required to evaluate its existing intangible assets and goodwill that were acquired in purchase business combinations and to make any necessary reclassifications in order to conform with the new classification criteria in SFAS No. 141 for recognition separate from goodwill. The Company assessed the useful lives and residual values of all intangible assets acquired, and made any necessary amortization period adjustments during the three-month period ended June 30, 2002. Intangible assets identified as having an indefinite useful life were tested for impairment in accordance with the provisions of SFAS No. 142.

In connection with the SFAS No. 142 transitional goodwill impairment evaluation, SFAS No. 142 requires the Company to perform an assessment of whether there is an indication that goodwill is impaired as of the date of adoption. To accomplish this, the Company determined it operated a single reporting unit and determined the carrying value of its reporting unit by assigning the assets and

liabilities, including the existing goodwill and intangible assets, to that reporting unit as of April 1, 2002. The Company had up to six months from April 1, 2002 to determine the fair value of its reporting unit and compare it to the carrying amount of the reporting unit. To the extent the carrying amount of a reporting unit exceeds the fair value of the reporting unit, an indication exists that the reporting unit goodwill may be impaired and the Company must perform the second step of the transitional impairment test. The second step is required to be completed as soon as possible, but no later than March 31, 2003, the end of the year of adoption. In the second step, the Company must compare the implied fair value of the reporting unit goodwill with the carrying amount of the reporting unit goodwill, both of which would be measured as of the date of adoption. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit to all of the assets (recognized and unrecognized) and liabilities of the reporting unit in a manner similar to a purchase price allocation, in accordance with SFAS No. 141. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill. Any transitional impairment loss will be recognized as the cumulative effect of a change in accounting principle in the Company's statement of operations.

As of March 31, 2002, the Company had unamortized goodwill in the amount of $26.8 million and unamortized identifiable intangible assets in the amount of $6.9 million, all of which were subject to the transition provisions of SFAS No. 142. Amortization expense of $650,000 was recorded during the three-month period ended December 31, 2002 related to amortization of intangible assets. Amortization is done on a straight-line basis over the estimated useful life of the underlying assets, estimated at four years. As of April 1, 2002, the Company had completed steps 1 and 2 of the transition provisions of SFAS No. 142. The Company identified one reporting unit and based on the Company's analysis of the fair value of its reporting unit as compared to its carrying value, the adoption of the impairment provisions of SFAS No. 142 did not have a material impact on the results of operations and no impairment existed as of April 1, 2002. The Company's primary assessment of the fair value of its reporting unit is based on its market capitalization at the time of the assessment. The Company will continue to assess for impairment at each fiscal year end or at any time it becomes aware of factors or circumstances that would warrant the assessment for impairment.

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The following table presents details of the Company's intangible assets and goodwill (in thousands):

	Gross Carrying Amount	Accumulated Amortization	Balance
December 31, 2002:			
Assets Subject to Amortization:			
Installed base, including core technology	$ 10,400	$ 5,417	$ 4,983
Assets not subject to amortization:			
Goodwill, including assembled workforce			$ 27,834
March 31, 2002			
Assets Subject to Amortization:			
Installed base, including core technology	$ 10,400	$ 3,467	$ 6,933
Assembled workforce	2,080	924	1,156
Goodwill	38,413	12,778	25,635
	$ 50,893	$ 17,169	$ 33,724

The following table reconciles changes to goodwill, including assembled workforce, for the nine-month period ended December 31, 2002 (in thousands):

Balance as of March 31, 2002	$ 26,791
Settlement of contingency based on earnings for General Automation acquisition	1,043
Balance as of December 31, 2002	$ 27,834

The Company had aggregate amortization expense of $650,000 and $1,950,000, respectively, for the three and nine-month periods ended December 31, 2002.

Estimated amortization expense for future periods is as follows (in thousands):

For the Year Ended:

March 31, 2003	$ 2,600
March 31, 2004	$ 2,600
March 31, 2005	$ 1,733
March 31, 2006	$
March 31, 2007	$

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The following table reconciles previously reported net loss as if the provisions of SFAS No. 142 were in effect in the prior fiscal year (unaudited in thousands except per share amounts):

	Three Months ended December 31, 2002	Three Months ended December 31, 2001	Nine Months ended December 31, 2002	Nine Months ended December 31, 2001
Reported net loss	$ (635)	$ (4,595)	$ (3,290)	$ (15,734)
Add back: Goodwill amortization, net of taxes		2,557		7,639
Adjusted net loss	(635)	(2,038)	(3,290)	(8,095)
Reported basic and diluted loss per common share	$ (0.04)	$ (0.29)	$ (0.19)	$ (0.96)
Add back: Goodwill amortization, net of taxes		0.16		0.47
Adjusted basic and diluted loss per common share	$ (0.04)	$ (0.13)	$ (0.19)	$ (0.49)

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations" ("SFAS No. 143"). SFAS No. 143 requires the Company to record the fair value of an asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the retirement of tangible long-lived assets that result from the acquisition, construction, development and/or normal use of the assets. The Company also records a corresponding asset, which is depreciated over the life of the asset. Subsequent to the initial measurement of the asset retirement obligation, the obligation will be adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The Company is required to adopt SFAS No. 143 on April 1, 2003, but does not expect adoption to have a material effect on its financial condition or results of operations.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS No. 144"). SFAS No. 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. SFAS No. 144 requires companies to separately report discontinued operations and extends that reporting to a component of an entity that either has been disposed of (by sale, abandonment, or in a distribution to owners) or is classified as held for sale. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. The Company adopted SFAS No. 144 on April 1, 2002. The Company has determined that the effect of the adoption of SFAS No. 144 had no material impact on its financial condition and results of operations.

In April 2002, the FASB issued SFAS No. 145, "Rescission of the FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections," ("SFAS No. 145"). SFAS No. 145 eliminates the requirement to classify gains and losses from the extinguishment of indebtedness

as extraordinary, requires certain lease modifications to be treated the same as a sale-leaseback transaction, and makes other non-substantive technical corrections to existing pronouncements. SFAS No. 145 is effective for fiscal years beginning after May 15, 2002. The Company expects the only impact, if any, of adopting SFAS No. 145 to be the reclassification of extraordinary losses to interest expense and income taxes if such extraordinary losses are incurred.

In July 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," ("SFAS No. 146"). SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. Examples of costs covered by the standard include lease termination costs and certain employee severance costs that are associated with a restructuring, discontinued operations, plant closing, or other exit or disposal activities. SFAS No. 146 is effective prospectively for exit or disposal activities initiated after December 31, 2002. Accordingly, SFAS No. 146 may affect the timing of recognizing future restructuring costs as well as the amounts recognized.

3. LONG-TERM DEBT

Long-term debt of the Company, including the Note Payable to Astoria Capital Partners, L.P. ("Astoria"), the Company's largest stockholder, as of December 31, 2002 and March 31, 2002 (in thousands):

	December 31, 2002	March 31, 2002
	(Unaudited)	
Note Payable to Astoria	$ 18,525	$ 18,525
Plus Accrued Interest	3,436	2,013
Less Unamortized Discount	(551)	(2,036)
	21,410	18,502
Notes Payable and Accrued Interest Other Stockholders		798
Note Payable and Accrued Interest Individual	256	250
Note Payable related to Asset Purchase		108
Note Payable Other	6	3
Capital Lease Obligations	118	48
Total Debt	21,790	19,709
Less Current Portion of Long-Term Debt	(326)	(1,207)
Total Long-Term Debt	$ 21,464	$ 18,502

As further explained in Note 5 below, in January 2003, the Company entered into a Note Exchange Agreement with Astoria replacing the Secured Promissory Note with a Convertible Subordinated Note that extended the maturity date to May 30, 2008. As such, the amount of principal, accrued interest and unamortized discount have been classified in the accompanying Unaudited Condensed Consolidated Balance Sheet as Long-Term Debt.

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4. STOCKHOLDERS' EQUITY

The Company's Earnings Per Share data and Dilutive Shares Outstanding exclude 146,764 shares and 1,338,032 shares for the three-month periods ended December 31, 2002 and 2001, respectively and 161,984 shares and 1,745,974 shares for the nine-month periods ended December 31, 2002 and 2001, respectively, as the effect of these shares, related to options and warrants, if exercised, would have been anti-dilutive.

The change in Accumulated Other Comprehensive Income during the three-month and nine-month periods ended December 31, 2002 and 2001 is the result of the effect of foreign exchange rate changes. The following table reconciles Net Loss as reported with Total Comprehensive Loss (in thousands):

	Three Months ended December 31,		Nine Months ended December 31,	
	2002	2001	2002	2001
Net Loss Reported	$ (635)	$ (4,595)	$ (3,290)	$ (15,734)
Translation Adjustments, Net	6	(4)	133	24
Total Comprehensive Loss	$ (629)	$ (4,599)	$ (3,157)	$ (15,710)

5. SUBSEQUENT EVENTS, COMMITMENTS AND CONTINGENCIES

As of December 31, 2002, Astoria held a Secured Promissory Note, dated November 30, 2000, as amended (the "Secured Promissory Note"), with a balance, excluding the unamortized note discount and including accrued interest, of $22.0 million. The Company assumed the Secured Promissory Note in connection with its acquisition of PickAx. In January 2003, the Company and Astoria entered into a Note Exchange Agreement (the "Exchange Agreement") to replace the existing Secured Promissory Note with a Convertible Subordinated Note. Under the terms of the Exchange Agreement, the Company issued to Astoria a Convertible Subordinated Note having a principal amount of $22.1 million, which principal amount is equal to the outstanding principal and accrued interest payable on the Secured Promissory Note as of the date of the Exchange Agreement. The Convertible Subordinated Note is convertible into Common Stock at a price of $5.00 per share. The Convertible Subordinated Note matures May 30, 2008, extending the May 30, 2003 maturity date of the Secured Promissory Note, and the interest rate is 5% per annum as compared to an interest rate of 10% per annum under the Secured Promissory Note. The interest is payable quarterly at the Company's option in cash or through increases to the outstanding principal of the Convertible Subordinated Note. Unlike the Secured Promissory Note, the Convertible Subordinated Note is not secured by the Company's assets.

In addition to holding the Convertible Subordinated Note, Astoria is a major stockholder of the Company, holding all of the Company's Preferred Stock and a majority of the outstanding Common Stock. Richard W. Koe, a member of the Company's Board of Directors, serves as the Managing General Partner for Astoria. Carlton H. Baab, the Company's President and Chief Executive Officer, served as a Managing Principal of Asto