J2 GLOBAL COMMUNICATIONS INC
Form 10-Q
August 09, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2005

OR

o 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: 0-25965

j2 GLOBAL COMMUNICATIONS, INC.
(Exact name of registrant as specified in its charter)

Delaware	**51-0371142**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

6922 Hollywood Boulevard
Suite 500
Los Angeles, California 90028
(Address of principal executive offices)

(323) 860-9200
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required 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 x No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).
Yes x No o

As of August 4, 2005, the registrant had 24,480,786 shares of Common Stock outstanding.

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j2 GLOBAL COMMUNICATIONS, INC.
FOR THE QUARTER ENDED JUNE 30, 2005

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

j2 Global Communications, Inc.
Condensed Consolidated Balance Sheets
(In thousands)

	June 30, 2005 (Unaudited)	December 31, 2004
ASSETS		
Cash and cash equivalents	$ 17,860	$ 18,814
Short-term investments	58,092	47,225
Accounts receivable, net of allowances of $767 and $529, respectively	9,530	8,227
Prepaid expenses and other current assets	2,124	2,873
Deferred income taxes	2,520	2,520
Total current assets	90,126	79,659
Long-term investments	32,625	27,753
Property and equipment, net	14,260	12,386
Goodwill	19,919	20,173
Other purchased intangibles, net	21,250	11,256
Other assets	175	170
Deferred income taxes	1,520	1,520
Total assets	$ 179,875	$ 152,917
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accounts payable and accrued expenses	$ 4,931	$ 5,324
Income taxes payable	2,605	192
Deferred revenue	5,835	5,378
Current portion of long-term debt	681	1,196
Total current liabilities	14,052	12,090
Long-term debt	491	866
Total liabilities	14,543	12,956
Total stockholders' equity	165,332	139,961
Total liabilities and stockholders' equity	$ 179,875	$ 152,917

See accompanying notes to condensed consolidated financial statements

j2 Global Communications, Inc.
Condensed Consolidated Statements of Operations
(Unaudited, in thousands except share and per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Revenues:				
Subscriber	$ 34,080	$ 25,063	$ 65,355	$ 47,125
Other	805	768	1,754	1,648
	34,885	25,831	67,109	48,773
Cost of revenues	6,912	5,133	13,409	9,938
Gross profit	27,973	20,698	53,700	38,835
Operating expenses:				
Sales and marketing	5,510	4,767	10,972	8,546
Research, development and engineering	1,663	1,264	3,424	2,314
General and administrative	5,464	3,664	10,609	6,981
Total operating expenses	12,637	9,695	25,005	17,841
Operating earnings	15,336	11,003	28,695	20,994
Interest and other income, net	733	352	1,330	538
Earnings before income taxes	16,069	11,355	30,025	21,532
Income tax expense	4,339	3,866	8,107	7,644
Net earnings	$ 11,730	$ 7,489	$ 21,918	$ 13,888
Net earnings per common share:				
Basic	$ 0.49	$ 0.32	$ 0.92	$ 0.60
Diluted	$ 0.46	$ 0.29	$ 0.86	$ 0.54
Weighted average shares outstanding:				
Basic	23,824,015	23,211,954	23,745,897	23,166,504
Diluted	25,430,940	25,584,617	25,422,974	25,524,611

See accompanying notes to condensed consolidated financial statements

j2 Global Communications, Inc.
Condensed Consolidated Statements of Cash Flows
(Unaudited, in thousands)

	Six Months Ended June 30, 2005	Six Months Ended June 30, 2004
Cash flows from operating activities:		
Net earnings	$ 21,918	$ 13,888
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	3,393	2,165
Compensation expense in exchange for note reduction	—	87
Tax benefit of stock option exercises	2,747	1,013
Deferred income taxes	—	6,013
Changes in assets and liabilities, net of effects of business acquisitions:		
Decrease (increase) in:		
Accounts receivable	(807)	(1,819)
Prepaid expenses	724	677
Other assets	28	(343)
(Decrease) increase in:		
Accounts payable and accrued expenses	(1,885)	975
Income taxes payable	2,413	—
Deferred revenue	458	640
Net cash provided by operating activities	28,989	23,296
Cash flows from investing activities:		
Net purchases of available-for-sale investments	(125)	(3,950)
Net purchases of held-to-maturity investments	(15,615)	(6,222)
Purchases of property and equipment	(3,893)	(1,761)
Acquisition of businesses, net of cash received	(7,467)	(6,198)
Purchases of intangible assets	(3,337)	(4,819)
Net cash used in investing activities	(30,437)	(22,950)
Cash flows from financing activities:		
Issuance of common stock under employee stock purchase plan	278	211
Exercise of stock options and warrants	1,781	367
Repayment of long-term debt	(883)	(834)
Net cash provided by (used in) financing activities	1,176	(256)
Effect of exchange rate changes on cash and cash equivalents	(682)	3
Net (decrease) increase in cash and cash equivalents	(954)	93
Cash and cash equivalents at beginning of period	18,814	32,882
Cash and cash equivalents at end of period	$ 17,860	$ 32,975

See accompanying notes to condensed consolidated financial statements

j2 GLOBAL COMMUNICATIONS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2005
(UNAUDITED)

NOTE 1 - BASIS OF PRESENTATION

j2 Global Communications, Inc. ("j2 Global" or the "Company") is a Delaware corporation founded in 1995. The Company leverages the power of the Internet to provide outsourced, value-added messaging and communications services to individuals and businesses throughout the world. j2 Global offers faxing and voicemail solutions; hosted email, email perimeter protection services (i.e., virus protection and spam detection) and broadcast email services; call management and conference calling; document management solutions; and a bundled suite of these services. j2 Global markets its services principally under the brand names eFax®, j2®, jConnect®, eFax Corporate®, eFax Pro™, UniFax™, Onebox®, Electric Mail®, jBlast®, eFax Broadcast™, eVoice®, M4 Internet™, jBlast®, PaperMaster® and others.

The consolidated financial statements include the accounts of j2 Global and its direct and indirect wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

The accompanying interim condensed consolidated financial statements and related financial schedules are unaudited. The Company's interim condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") including those for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X issued by the Securities and Exchange Commission ("SEC"). Accordingly, they do not include all of the information and note disclosures required by GAAP for complete financial statements. These statements are unaudited and, in the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been reflected in these condensed consolidated financial statements. These consolidated financial statements should be read in conjunction with the audited financial statements and related notes for the year ended December 31, 2004 included in the Company's Annual Report on Form 10-K filed with the SEC on March 28, 2005.

The results of operations for these interim periods are not necessarily indicative of the operating results for the full year or for any future period.

Certain prior year reported amounts have been reclassified to conform with the current year presentation. Included in these reclassifications were auction rate securities in the amount of $14.0 million and $18.0 million as of December 31, 2003 and June 30, 2004, respectively, which have been reclassified from cash equivalents to short-term investments in the accompanying consolidated statement of cash flows. The reclassification had the effect of increasing the net purchases of available-for-sale investments, increasing net cash used in investing activities, and decreasing the net increase in cash and cash equivalents each by $4.0 million from the amounts previously reported on the consolidated statement of cash flows for the six months ended June 30, 2004.

Comprehensive income was approximately $20.6 million and $13.9 million for the six months ended June 30, 2005 and 2004, respectively. The components of comprehensive income were net earnings and accumulated other comprehensive income. The change in accumulated other comprehensive income for all periods presented resulted from foreign currency translation gains and losses. Net translation losses for the six months ended June 30, 2005 and 2004 were $1.4 million and zero, respectively. Taxes have not been provided for foreign currency translation gains and losses as the Company intends to reinvest the undistributed earnings of its foreign subsidiaries.

NOTE 2 - ACCOUNTING FOR STOCK OPTIONS

The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees", and related interpretations to account for its fixed plan stock options. These interpretations include Financial Accounting Standards Board ("FASB") Interpretation No. 44, "Accounting for Certain Transactions involving Stock Compensation an interpretation of APB Opinion No. 25", issued in March 2000. Under this method, compensation expense is generally recorded on the date

of grant only if the current market price of the underlying stock exceeded the exercise price. SFAS No. 123, "Accounting for Stock-Based Compensation", established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic value-based method of accounting described above, and has adopted the disclosure requirements of SFAS No. 123.

The Company accounts for option grants to non-employees using the guidance of SFAS No. 123 and Emerging Issues Task Force ("EITF") No. 96-18, whereby the fair value of such options is determined using the Black-Scholes option pricing model at the earlier of the date at which the non-employee's performance is complete or a performance commitment is reached.

The Company applies APB Opinion No. 25 in accounting for stock options and, accordingly, no compensation cost using the intrinsic value method has been recognized for stock options granted to employees in the accompanying financial statements. If the fair value based method had been applied in measuring stock compensation expense under SFAS No. 123, the pro forma effect on net earnings and net earnings per share would have been as follows:

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2005	**2004**	**2005**	**2004**
	(In thousands, except per share data)			
Net earnings, as reported	$ 11,730	$ 7,489	$ 21,918	$ 13,888
Deduct: Stock-based employee compensation expense determined under the fair value-based method for all awards, net of related tax effect	(675)	(336)	(1,350)	(823)
Pro forma net earnings	$ 11,055	$ 7,153	$ 20,568	$ 13,065
Basic net earnings per common share:				
As reported	$ 0.49	$ 0.32	$ 0.92	$ 0.60
Pro forma	$ 0.46	$ 0.31	$ 0.87	$ 0.56
Diluted net earnings per common share:				
As reported	$ 0.46	$ 0.29	$ 0.86	$ 0.54
Pro forma	$ 0.44	$ 0.28	$ 0.81	$ 0.51

In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment", which stated SFAS 123R was effective for the interim or annual periods beginning after June 15, 2005. However, on April 15, 2005, the SEC issued Final Rule No. 33-8568, "Amendment to Rule 4-01(a) of Regulation S-X Regarding the Compliance Date for Statement of Financial Accounting Standards No. 123 (Revised 2004), *Share Based Payment*". The SEC's new rule allows companies to implement SFAS 123R at the beginning of their next fiscal year, instead of the next reporting period, that begins after June 15, 2005. SFAS 123R therefore becomes effective for the Company in the first quarter of fiscal 2006. Statement 123R requires all share-based payments to employees, including grants of employee stock options and purchases under employee stock purchase plans, to be recognized as an operating expense in the income statement. The cost is recognized over the requisite service period based on fair values measured on grant dates, and the new standard may be adopted using either the "modified prospective transition" method or the "modified retrospective transition" method. The Company is currently evaluating the effect that the adoption of SFAS 123R will

have on the Company's consolidated statement of income and financial condition.

NOTE 3 - USE OF ESTIMATES

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of net revenue and expenses during the reporting period. On an ongoing basis, management evaluates its estimates, including those related to revenue recognition, allowances for doubtful accounts and the valuation of deferred income taxes, long-lived and intangible assets and goodwill. These estimates are based on

historical experience and on various other factors that management believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results could differ from those estimates.

NOTE 4 - RECENT ACCOUNTING PRONOUNCEMENTS

In March 2004, the EITF reached a consensus on Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" ("EITF 03-1"). EITF 03-1 provides guidance for determining when an investment is other-than-temporarily impaired to be applied in reporting periods beginning after June 15, 2004 and contains disclosure requirements effective in annual financial statements for fiscal years ending after December 15, 2003 for investments accounted for under SFAS Nos. 115 and 124. For all other investments within the scope of this Issue, the disclosures are effective for fiscal years ending after June 15, 2004. In September 2004, the FASB delayed the accounting provisions of EITF 03-1; however, the disclosure requirements remain effective. In June 2005, the FASB decided not to provide additional guidance on the meaning of other-than-temporary impairment, and directed the staff to issue proposed FSP EITF 03-1a, "Implementation Guidance for the Application of Paragraph 16 of EITF Issue No. 03-1" which in its final form will be retitled FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." The Company has evaluated the impact of the adoption of EITF 03-1 and does not believe it will have a material effect on the Company's financial condition or results of operations.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets — An Amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions". SFAS 153 eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in paragraph 21(b) of APB Opinion No. 29, "Accounting for Nonmonetary Transactions," and replaces it with an exception for exchanges that do not have commercial substance. SFAS 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. This standard is effective for fiscal periods beginning after June 15, 2005. The Company is currently evaluating the effect that the adoption of SFAS 153 will have on the Company's consolidated statement of income and financial condition.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections". SFAS 154 applies to all voluntary changes in accounting principle and changes the accounting for and reporting of a change in accounting principle. SFAS 154 requires retrospective application to prior periods' financial statements of a voluntary change in accounting principle unless it is impracticable and requires that a change in method of depreciation, amortization, or depletion for long-lived, nonfinancial assets be accounted for as a change in accounting estimate that is effected by a change in accounting principle. This standard is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The Company is currently evaluating the effect that the adoption of SFAS 154 will have on the Company's consolidated statement of income and financial condition.

In June 2005, the EITF reached a consensus on Issue No. 05-6, "Determining the Amortization Period for Leasehold Improvements" ("EITF 05-6"). EITF 05-6 provides guidance that leasehold improvements acquired in a business combination or purchased subsequent to the inception of the lease should be amortized over the lesser of the useful life of the asset or the lease term that includes reasonably assured lease renewals as determined on the date of the acquisition of the leasehold improvement. The guidance should be applied prospectively and reasonably assured lease renewals should be considered in determining the amortization period of leasehold improvements acquired (either directly or in business combinations) in periods beginning after June 29, 2005. The Company is currently evaluating the effect that the adoption of EITF 05-6 will have on the Company's consolidated statement of income and financial condition.

NOTE 5 - EARNINGS PER COMMON SHARE

Basic earnings per share is computed on the basis of the weighted average number of common shares outstanding. Diluted earnings per share is computed on the basis of the weighted average number of common shares outstanding plus the effect of outstanding stock options and warrants using the “treasury stock” method. The components of basic and diluted earnings per share are as follows:

	Three Months Ended June 30, 2005	Three Months Ended June 30, 2004	Six Months Ended June 30, 2005	Six Months Ended June 30, 2004
	(In thousands, except share and per share data)			
Numerator for basic and diluted net earnings per common share:				
Net earnings	$ 11,730	$ 7,489	$ 21,918	$ 13,888
Denominator:				
Weighted average outstanding shares of common stock	23,824,015	23,211,954	23,745,897	23,166,504
Dilutive effect of:				
Employee stock options	1,442,090	2,078,497	1,494,924	2,065,314
Warrants	164,835	294,166	182,153	292,793
Common stock and common stock equivalents	25,430,940	25,584,617	25,422,974	25,524,611
Net earnings per share:				
Basic	$ 0.49	$ 0.32	$ 0.92	$ 0.60
Diluted	$ 0.46	$ 0.29	$ 0.86	$ 0.54

NOTE 6 - ACQUISITIONS

During the six months ended June 30, 2005, the Company completed two acquisitions neither of which were material to the Company's financial position at the date of acquisition. In the first acquisition, the Company purchased substantially all of the assets and operations of a European provider of fax-to-email and unified messaging services. In the second acquisition, the Company purchased substantially all of the assets and operations of a California provider of fax-to-email and unified messaging services. The aggregate purchase price, including acquisition costs, for these two acquisitions was $7.8 million, payable in cash at closing, with a contingent holdback based on working capital requirements with respect to one of the acquisitions. The transactions have been accounted for using the purchase method and, accordingly, the results of operations for these acquisitions have been included in the consolidated results of the Company since the date of acquisition. The excess of the aggregate purchase price over the fair value of identifiable net assets acquired amounted to $7.7 million. As of the date of this report, the Company has not completed the allocation of excess aggregate purchase price between goodwill and identifiable intangible assets. The results of operations for these acquisitions during periods prior to the acquisition date were not material to the Company's consolidated results of operations and accordingly, pro forma results of operations have not been prepared.

NOTE 7 - GOODWILL AND PURCHASED INTANGIBLE ASSETS

Goodwill represents the excess of the purchase price over the fair value of the net tangible and identifiable intangible assets acquired in a business combination. Intangible assets resulting from the acquisitions of entities accounted for using the purchase method of accounting are estimated by management based on the fair value of assets acquired. Identifiable intangible assets subject to amortization are being amortized using the straight-line method over estimated useful lives ranging from two to twenty years.

The changes in carrying amount of goodwill and other intangible assets for the six months ended June 30, 2005 are as follows (in thousands):

	Balance as of	Foreign Exchange	Balance as of

	January 1, 2005	Additions	Amortization	Translation	June 30, 2005
Goodwill	$ 20,173	$ 200	$ —	$ (454)	$ 19,919
Intangible assets with indefinite lives	1,409	64	—	—	1,473
Intangible assets subject to amortization	9,847	3,314	(870)	(216)	12,075
Other - unallocated (refer to Note 6)	—	7,702	—	—	7,702
Total	$ 31,429	$ 11,280	$ (870)	$ (670)	$ 41,169

Intangible assets with indefinite lives relate primarily to a trade name. As of June 30, 2005, intangible assets subject to amortization relate primarily to the following (in thousands):

	Weighted-Average Amortization period	Historical cost	Accumulated amortization	Net
Patents	10.39 years	$ 9,806	$ (1,060)	$ 8,746
Technology	2.08 years	2,843	(2,718)	125
Customer relationships	4.88 years	2,095	(523)	1,572
Trade name	20 years	1,710	(78)	1,632
Total		$ 16,454	$ (4,379)	$ 12,075

Amortization expense, included in general and administrative expense, during the six-month periods ended June 30, 2005 and 2004 approximated $870,000 and $230,000, respectively. Amortization expense is estimated to approximate $1.7 million, $1.6 million, $1.5 million, $1.5 million and $1.3 million for fiscal years 2005 through 2009, respectively.

NOTE 8 - INCOME TAXES

Income tax expense amounted to approximately $4.3 million and $3.9 million for the three months ended June 30, 2005 and 2004, respectively. For the six months ended June 30, 2005 and 2004, income tax expense was $8.1 million and $7.6 million, respectively. During the six months ended June 30, 2004, deferred income taxes decreased by $6.0 million primarily due to the offset of the Company’s tax liability against available net operating loss and tax credit carry-forwards.

Income tax expense for the three and six months ended June 30, 2005 is based on our worldwide estimated effective annual tax rate of approximately 27%.

NOTE 9 - SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest during the six-month periods ended June 30, 2005 and 2004 approximated $39,000 and $33,000, respectively, substantially all of which related to long-term debt.

The Company paid approximately $2.1 million and $787,000, respectively, for federal, state and foreign income taxes during the six-month periods ended June 30, 2005 and 2004.

In the second quarter of 2004, the Company entered into a loan arrangement totaling approximating $100,000 to finance a corporate insurance policy.

During the six months ended June 30, 2004, the Company entered into capital lease arrangements for certain computer equipment and software totaling approximately $168,000.

Through the six months ended June 30, 2005 and 2004, the Company recorded the tax benefit from the exercise of non-qualifying stock options and disqualifying dispositions of incentive stock options as a reduction of its income tax liability and an increase in equity in the amount of approximately $2.7 million and $1.0 million, respectively.

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

ORGANIZATION AND DESCRIPTION OF BUSINESS

j2 Global Communications, Inc. ("j2 Global", "our" or "we") is a Delaware corporation founded in 1995. The Company leverages the power of the Internet to provide outsourced, value-added messaging and communications services to individuals and businesses throughout the world. We offer faxing and voicemail solutions; hosted email, email perimeter protection services (i.e., virus protection and spam detection) and broadcast email services; call management and conference calling; document management solutions; and a bundled suite of these services. We market our services principally under the brand names eFax®, j2®, jConnect®, eFax Corporate®, eFax Pro™, UniFax™, Onebox®, Electric Mail®, jBlast®, eFax Broadcast™, eVoice®, M4 Internet™, jBlast®, PaperMaster® and others.

We deliver many of our services through our global telephony/Internet Protocol ("IP") network, which covers more than 1,500 cities in 25 countries across five continents. We have created this network, and continuously seek to expand it, through negotiating with U.S. and foreign telecommunications and co-location providers for telephone numbers (also referred to as Direct Inward Dial numbers or "DIDs"), Internet bandwidth and co-location space for our equipment. We maintain and seek to grow an inventory of telephone numbers to be assigned to new customers. Most of these numbers are "local" (as opposed to toll-free), which enables us to provide our paying subscription customers telephone numbers with a geographic identity.

Our core services include fax, voicemail, email, call management and conference calling and a bundled suite of these services. These are business services that enable our customers to be more efficient, more mobile, more cost-effective and more secure than traditional alternatives. We generate substantially all of our revenue from subscribers that pay activation, subscription and usage fees. We also generate revenue from advertising and revenue-share on premium rate international DIDs issued to non-paid subscribers (sometimes referred to as "Free" subscribers). Of the more than 9.3 million telephone numbers (or DIDs) deployed as of June 30, 2005, approximately 642,000 were serving paying subscribers, with the balance deployed to Free subscribers.

We operate in one reportable segment: value-added messaging and communications services, which provides for the delivery of fax, voice and email messages via the telephone and/or Internet networks. Our services are distributed worldwide primarily over the telephone and Internet networks, and thus, we do not consider our operations subject to any geographic segment reporting.

We generate a substantial portion of our revenues from subscribers that pay us for activation, subscription and usage fees. Activation and subscription fees are referred to as "fixed" revenues, while usage fees are referred to as "variable" revenues. We also generate a small percentage of our overall revenue from advertising and international "calling party pays" arrangements to Free subscribers. These Free advertising-supported subscribers also serve as a source for attracting new paid subscribers and provide us a cost-effective method for mass-marketing our eFax and jConnect services. This process of migrating advertising-supported customers to paid services is part of our life cycle management program. Through this program, we monitor usage levels of advertising-supported customers, send them promotional up-sell messages and cull out subscribers that do not adhere to the limitations on our Free services set forth in our customer agreements.

During the past three years, we have derived a substantial portion of our revenues from the sale of our eFax and jConnect paid services, including eFax Corporate®, eFax Plus® and jConnect Premier®. These services are deployed through a DID. As a result, we believe that paying DIDs and the revenues associated therewith are an important metric for understanding our business. It has been and continues to be our objective to increase the number of paying DIDs through a variety of distribution channels, marketing arrangements and enhanced brand awareness. In addition, we continuously seek to increase revenues through a combination of stimulating use by our customers of usage-based

services, introduction of new services and instituting appropriate price increases to our fixed monthly subscription and other fees.

The following table sets forth key operating metrics of our Company for the three and six months ended June 30, 2005 and 2004:

	June 30, 2005	June 30, 2004
	(In thousands)	
Free service telephone numbers	8,653	6,873
Paying telephone numbers	642	469
Total active telephone numbers	9,295	7,342

	Three Months Ended June 30, 2005	Three Months Ended June 30, 2004	Six Months Ended June 30, 2005	Six Months Ended June 30, 2004
	(In thousands except percentages and average revenue per paying telephone number)			
Subscriber revenues:				
Fixed	$ 23,757	$ 17,750	$ 46,530	$ 33,770
Variable	10,323	7,313	18,825	13,355
Total subscriber revenues	$ 34,080	$ 25,063	$ 65,355	$ 47,125
Percentage of total subscriber revenues:				
Fixed	69.7%	70.8%	71.2%	71.7%
Variable	30.3%	29.2%	28.8%	28.3%
Revenues:				
DID based	$ 33,009	$ 24,057	$ 63,195	$ 45,721
Non-DID based	1,876	1,774	3,914	3,052
Total revenues	$ 34,885	$ 25,831	$ 67,109	$ 48,773
Average monthly revenue per paying telephone number[1]	$ 17.21	$ 17.22		

[1] See calculation of average monthly revenue per paying telephone number at the end of this section, Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

DISCUSSION OF CRITICAL ACCOUNTING POLICIES AND ESTIMATES

In the ordinary course of business, we have made a number of estimates and assumptions relating to the reporting of results of operations and financial condition in the preparation of our financial statements. Actual results could differ significantly from those estimates under different assumptions and conditions. During the six months ended June 30, 2005, there have been no changes in the Company’s critical accounting policies described in the Company’s Annual Report on Form 10-K filed with the SEC on March 28, 2005.

RESULTS OF OPERATIONS FOR THE THREE- AND SIX-MONTH PERIODS ENDED JUNE 30, 2005 AND 2004

Revenues

Subscriber Revenues. Subscriber revenues consist of both a fixed monthly recurring subscription component and a variable component which is driven by the actual usage of the service offerings. We have only tracked this ratio since fiscal year 2003, so data is not available prior to 2003. Over the past ten quarters, the fixed portion of our subscriber revenues has consistently contributed approximately 70% to our subscriber revenues. Subscriber revenues were $34.1 million and $25.1 million for the three months ended June 30, 2005 and 2004, respectively. For the six months ended June 30, 2005 and 2004, subscriber revenues were $65.4 million and $47.1 million, respectively. The increase in subscriber revenues was due to an increase in our base of paying subscribers. We obtained these additional paid subscribers primarily from new sign-ups from subscribers coming directly to our websites, Free-to-Paid subscriber upgrades, small to mid-sized corporate sales, direct large enterprise and government sales and direct marketing spend for Paid subscribers, net of cancellations.

Other Revenues. Other revenues were $805,000 and $768,000 for the three months ended June 30, 2005 and 2004, respectively. For the six months ended June 30, 2005 and 2004, other revenues were $1.8 million and $1.6 million, respectively. Other revenues consist primarily of advertising revenues generated by delivering email messages and banners on behalf of advertisers to our Free customers and the sale of our PaperMaster Pro document management software.

For the past three years, 90% or more of our total revenues have been produced by our DID-based services. DID-based revenues increased from $24.1 million to $33.0 million for the three-month periods ended June 30, 2004 and 2005, respectively. For the six months ended June 30, 2005 and 2004, DID-based revenues were $63.2 million and $45.7 million, respectively. The primary reason is the increase in the number of paid DIDs over this period. We would expect that DID-based revenues to continue to be a dominant driver of total revenues.

Cost of Revenues. Cost of revenues are primarily comprised of costs associated with data and voice transmission, telephone numbers, network operations, customer service, on-line processing fees and equipment depreciation. Cost of revenues was $6.9 million, or 20% of total revenues, and $5.1 million, or 20% of total revenues, for the three months ended June 30, 2005 and 2004, respectively. For the six months ended June 30, 2005 and 2004, cost of revenues was $13.4 million, or 20% of total revenues, and $9.9 million, or 20% of total revenues, respectively. The increase in cost of revenues was due primarily to costs incurred in building and expanding our network infrastructure, enhancing and growing our customer support services and incurring increased variable transmission costs associated with a larger subscriber base and increased usage. Cost of revenues as a percentage of revenues remained fairly consistent year-over-year. For the balance of 2005, we expect cost of revenues as a percentage of revenues to be relatively stable.

Operating Expenses

Sales and Marketing. Our sales and marketing costs consist primarily of payments to sales and marketing personnel, advertising expenses and other business development related expenses. Sales and marketing expenses were $5.5 million, or 16% of total revenues, and $4.8 million, or 19% of total revenues, for the three months ended June 30, 2005 and 2004, respectively. For the six months ended June 30, 2005 and 2004, sales and marketing expenses were $11.0 million, or 16% of total revenues, and $8.5 million, or 18% of total revenues, respectively. The increase in sales and marketing expenses was due primarily to increased Internet-based advertising and partner marketing spend and additional marketing personnel. Our Internet-based advertising relationships consist primarily of fixed cost and performance-based (cost-per-impression, cost-per-click and cost-per-acquisition) advertising relationships with an array of online service providers. Throughout 2004 and the first half of 2005, we experienced upward pricing pressure for certain Internet-based advertising. We have a return on investment discipline-based approach to our Internet-based advertising and partner marketing spend which will cause sales and marketing costs as a percentage of total revenues to vary quarter-to-quarter.

Research, Development and Engineering. Our research, development and engineering costs consist primarily of personnel-related expenses. Research, development and engineering costs were $1.7 million, or 5% of total revenues, and $1.3 million, or 5% of total revenues, for the three months ended June 30, 2005 and 2004, respectively. For the six months ended June 30, 2005 and 2004, research, development and engineering costs were $3.4 million, or 5% of total revenues, and $2.3 million, or 5% of total revenues, respectively. The increase in research, development and engineering costs was primarily due to an increase in personnel costs to maintain our existing services, accommodate our service enhancements, develop and implement additional service features and functionality and continue to bolster our infrastructure security. Research, development and engineering costs as a percentage of revenues remained fairly consistent year-over-year. For the remainder of 2005, we expect research, development and engineering costs as a percentage of revenues to be relatively stable.

General and Administrative. Our general and administrative costs consist primarily of personnel-related expenses, depreciation and amortization, bad debt expense and insurance costs. General and administrative costs were $5.5

million, or 16% of total revenues, and $3.7 million, or 14% of total revenues, for the three months ended June 30, 2005 and 2004, respectively. For the six months ended June 30, 2005 and 2004, general and administrative costs were $10.6 million, or 16% of total revenues, and $7.0 million, or 14% of total revenues, respectively. The increase in general and administrative expenses was primarily attributable to a combination of increased depreciation and amortization due to additional property and equipment and intangible assets, increased bad debt

expense due to a growing customer base, additional personnel due to internal growth and acquisitions, and increased professional and consulting fees primarily related to compliance with the Sarbanes-Oxley Act of 2002. For the remainder of 2005, we expect general and administrative expenses as a percentage of revenue to remain relatively stable excluding any incremental amortization expense of intangible assets from any future acquisitions and assuming no relevant change in accounting or related compliance standards.

Interest and Other Income, Net. This income is generated primarily from interest income earned on cash, cash equivalents and short- and long-term investments, offset primarily by interest expense on long-term debt. Interest and other income, net amounted to $733,000 and $352,000 for the three months ended June 30, 2005 and 2004, respectively, and $1.3 million and $538,000 for the six months ended June 30, 2005 and 2004, respectively. The increase in interest and other income, net was primarily due to higher cash and investment balances and higher interest rates period-over-period.

Income Taxes. Our effective tax rate is based on pre-tax income, statutory tax rates, tax regulations and different tax rates in the various jurisdictions in which we operate. Income tax expense amounted to approximately $4.3 million and $3.9 million for the three months ended June 30, 2005 and 2004, respectively. For the six months ended June 30, 2005 and 2004, income tax expense was $8.1 million and $7.6 million, respectively. Income tax expense for the six months ended June 30, 2005 is based on a worldwide estimated effective annual tax rate for 2005 of approximately 27%. Our effective annual tax rate was approximately 33% for 2004. The decrease in our effective annual tax rate from 2004 to 2005 was due to an increased percentage of our income being sourced from lower tax jurisdictions.

Liquidity and Capital Resources

At June 30, 2005, we had cash and cash equivalents of $17.9 million, short-term investments of $58.1 million and $32.6 million of long-term investments. Our investments are comprised primarily of readily marketable corporate debt securities, U.S. government agency securities, and auction rate debt and preferred securities. For financial statement presentation, we classify our investments as short-term and long-term based upon their maturity dates. Short-term investments primarily mature within one year of the date of the financial statements and long-term investments mature between one and two years from June 30, 2005. We classify auction rate securities as short-term investments as the established interest rate reset periods are less than one year.

Our primary sources of liquidity are cash flows generated from operations, together with cash and cash equivalents and short-term investments. We generate our cash primarily from payments received from our subscribers, offset by cash payments we make to third parties for their services, employee compensation and capital expenditures. Net cash provided by operating activities was $29.0 million and $23.3 million for the six months ended June 30, 2005 and 2004, respectively. More than two-thirds of our subscriber revenues are paid by credit card and therefore our receivables from subscribers settle quickly. Allocations of our total cash and cash equivalents and short- and long-term investments on hand will generally vary during any given reporting period based on our short-term working capital requirements and return on investment opportunities. Our cash and cash equivalents and short-term investments were $76.0 million at June 30, 2005.

Net cash used in investing activities was approximately $30.4 million and $23.0 million for the six months ended June 30, 2005 and 2004, respectively. For the first half of 2005, net cash used in investing activities was primarily attributable to net purchases of investments, acquisition of businesses, purchases of property and equipment and purchases of intangible assets. For the first half of 2004, net cash used in investing activities was primarily comprised of purchases of investments and acquisition of businesses.

Net cash provided by financing activities of approximately $1.2 million was primarily comprised of proceeds from the exercise of stock options and warrants, and sale of common shares issued under our employee stock purchase plan, offset by repayments of long-term debt. Net cash used in financing activities of $256,000 for the six months ended

June 30, 2004 was primarily comprised of repayments of long-term debt, offset by proceeds from the exercise of stock options and sale of common shares issued under our employee stock purchase plan.

For 2004 and in prior years, our cash payments related to the accrual of income tax expense were substantially offset by net operating losses and tax credit carryforwards. As of December 31, 2004, our usable

federal NOLs and tax credit carryforwards were approximately $2.3 million and $2.3 million, respectively, and our usable state NOLs and tax credit carryforwards were approximately $10.2 million and $192,000, respectively. These usable federal and state NOLs were substantially exhausted in the first quarter of 2005. As a result, for 2005 we expect the amount of our cash tax payments primarily to depend upon the number of stock options exercised, which generally reduce taxable income.

We currently anticipate that our existing cash and cash equivalents and short-term investment balances will be sufficient to meet our anticipated needs for working capital and capital expenditures for at least the next 12 months.

FORWARD-LOOKING INFORMATION

In addition to historical information, the foregoing Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements. These forward-looking statements involve risks, uncertainties and assumptions. The actual results may differ materially from those anticipated in these forward-looking statements as a result of many factors, including but not limited to those discussed below, the results of any acquisition we may complete and the factors discussed in the section in this Quarterly Report on Form 10-Q entitled "Quantitative and Qualitative Disclosures About Market Risk". Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's opinions only as of the date hereof. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements. Readers should carefully review the risk factors described below, those identified in the "Risk Factors" section of our Annual Report on Form 10-K filed with the Securities and Exchange Commission ("SEC") on March 28, 2005 and the risk factors set forth in other documents we file from time to time with the SEC.

Some factors that could cause actual results to differ materially from those anticipated in these forward-looking statements include, but are not limited to, our ability to:

o Sustain growth or profitability;

o Continue to maintain, expand and retain our customer base;

o Compete with other similar providers with regard to price, service and functionality;

o Cost-effectively procure large quantities of telephone numbers in desired locations in the United States and abroad;

o Achieve business and financial objectives in light of burdensome telecommunications or Internet regulation;

o Obtain large quantities of non-paying users on a cost effective basis, and effectively derive revenues from those users through advertising to them and selling them paid services;

o Successfully manage our cost structure, including but not limited to our telecommunication and personnel related expenses;

o Successfully adapt to technological changes in the messaging, communications and document management industries;

o Successfully protect our intellectual property and avoid infringing upon the proprietary rights of others;

o Adequately manage growth in terms of managerial and operational resources;

o

Maintain and upgrade our systems and infrastructure to deliver acceptable levels of service quality and security of customer data and messages;

- o Introduce new services and achieve acceptable levels of returns-on-investment for those new services; and

o Recruit and retain key personnel.

Calculation of Average Revenue per Paying Telephone Number:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	**2004**	**2005**	**2004**
	(In thousands except average monthly revenue per paying telephone number)			
DID-based revenues	$ 33,009	$ 24,057	$ 63,195	$ 45,721
Less other revenues	994	707	2,060	1,488
Total paying telephone number revenues	$ 32,015	$ 23,350	$ 61,135	$ 44,233
Average paying telephone number monthly revenue (total divided by number of months)	$ 10,672	$ 7,783	$ 10,189	$ 7,372
Number of paying telephone numbers				
Beginning of period	598	435	554	400
End of period	642	469	642	469
Average of period	620	452	598	435
Average monthly revenue per paying telephone number[1]	$ 17.21	$ 17.22	$ 17.04	$ 16.96

[1]Due to rounding, individual numbers may not recalculate.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The following discussion of the market risks we face contains forward-looking statements. Forward-looking statements are subject to risks and uncertainties. Actual results could differ materially from those discussed in the forward-looking statements.

We believe that our exposure to market risk related to changes in interest rates and foreign currency exchange rates is not significant, primarily because our indebtedness under financing arrangements has fixed interest rates and our transactions are substantially denominated in US Dollars. During the balance of 2005 and in future years, we believe we will expand our international customer base and, as a result, we expect a greater level of foreign currency market risk.

We invest our cash primarily in high-grade interest-bearing securities. Our return on these investments is subject to interest rate fluctuations.

We do not have derivative financial instruments for hedging, speculative or trading purposes.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports 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 principal executive and principal financial officers, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Our disclosure controls and procedures are designed to provide a reasonable level of assurance of reaching our designed disclosure control objectives.

As of the end of the period covered by this report, j2 Global's management, with the participation of Scott M. Jarus, our principal executive officer and R. Scott Turicchi, our principal financial officer, carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934). Based upon that evaluation, Messrs. Jarus and Turicchi concluded that these disclosure controls and procedures were effective as of the end of the period covered in this report.

(b) Changes in Internal Controls

There was no change in internal control over financial reporting that occurred during the first half of 2005 that has materially affected or is reasonably likely to materially affect j2 Global's internal control over financial reporting except that in January 2005, the Company implemented a new accounting software application and certain business processes and accounting procedures have been modified as a result of this new system. In addition, the Company purchased a new fixed asset tracking system which it will be implementing throughout 2005. This system will improve the Company's visibility into the physical location of its assets and their valuation at any moment in time.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are not currently aware of any legal proceedings or claims that we believe are likely to have a material adverse effect on our business, prospects, financial condition, results of operations or cash flows.

Overview of Offensive Patent Litigation

As part of our continuing effort to prevent the unauthorized use of our intellectual property, we have initiated litigation against five companies for infringing our patents. Although we believe that we have a reasonable basis to prevail in each of these cases, patent litigation is inherently uncertain and there can be no assurances that we will prevail. These lawsuits are described below:

Venali, Inc. We have pending lawsuits against Venali, Inc. ("Venali") in the United States District Court for the Central District of California for infringement of several of our patents. The first complaint was filed in February 2004. We are seeking a reasonable royalty for the infringement of these patents, treble damages for the willful infringement of certain of these patents, a permanent injunction against continued infringement of these patents and attorney's fees, interest and costs. Venali has counterclaimed for a declaratory judgment of invalidity and non-infringement of these patents and seeks attorneys' fees, interest and costs. The cases are now in discovery. Reexamination proceedings on two of the several patents in suit are pending with the U.S. Patent and Trademark Office.

CallWave, Inc. We also have pending lawsuits against CallWave, Inc. ("CallWave") in the United States District Court for the Central District of California for infringement of several of our patents. The first complaint was filed in August 2004. We are seeking a reasonable royalty for the infringement of these patents, treble damages

for the willful infringement of certain of these patents, a permanent injunction against continued infringement of these patents and attorney's fees, interest and costs. CallWave has asserted affirmative defenses, counterclaimed for a declaratory judgment of invalidity and non-infringement and seeks attorneys' fees, interest and costs. The cases are now in discovery. A reexamination proceeding on one of the several patents in suit is pending with the U.S. Patent and Trademark Office.

Others. In addition to the cases above, during the third quarter of 2005 we have filed patent infringement lawsuits against EasyTEL Communications, Inc., Mijanda, Inc., and Protus IP Solutions Inc., all in the United States District Court for the Central District of California. In each case we are seeking a reasonable royalty for the infringement of the patent(s) in suit, a permanent injunction against continued infringement and attorney's fees, interest and costs. Each of these cases is in the preliminary stages.

Item 4. Submission of Matters to a Vote of Security Holders

Our 2005 Annual Meeting of Shareholders was held on May 4, 2005 in Los Angeles, California. There were 23,727,460 shares of our common stock entitled to be voted on March 23, 2005, the record date for the meeting. The following matter was submitted to our shareholders for a vote at the Annual Meeting:

To elect the following five directors nominees to serve for the ensuing year and until their successors are elected and qualified. All nominees were elected as directors with the following vote:

Nominee	Votes Received	Withheld or Abstained
Douglas Y. Bech	20,556,460	1,156,702
Robert J. Cresci	20,472,797	1,240,365
Richard S. Ressler	17,737,945	3,975,217
John F. Rieley	17,680,079	4,033,083
Michael P. Schulhof	20,572,422	1,140,740

Item 6. Exhibits

31(a) Rule 13a-14(a) Certification of Principal Executive Officer in accordance with Section 302 of the Sarbanes-Oxley Act of 2002

31(b) Rule 13a-14(a) Certification of Principal Financial Officer in accordance with Section 302 of the Sarbanes-Oxley Act of 2002

32(a) Section 1350 Certification of Principal Executive Officer in accordance with Section 906 of the Sarbanes-Oxley Act of 2002.

32(b) Section 1350 Certification of Principal Financial Officer in accordance with Section 906 of the Sarbanes-Oxley Act of 2002.

Items 2, 3 and 5 are not applicable and have been omitted.

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.

j2 Global Communications, Inc.

Date: August 8, 2005

By: /s/ R. SCOTT TURICCHI

R. Scott Turicchi
Chief Financial Officer
(Principal Financial Officer)

Date: August 8, 2005

By: /s/ GREGGORY KALVIN

Greggory Kalvin
Chief Accounting Officer
(Principal Accounting Officer)

INDEX TO EXHIBITS

ExhibitNumber	Description
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32(b)	Certification of Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.