BOINGO WIRELESS INC
Form 10-Q
November 12, 2013
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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 September 30, 2013

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: 001-35155

BOINGO WIRELESS, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**95-4856877** (I.R.S. Employer Identification No.)
10960 Wilshire Blvd., Suite 800 **Los Angeles, California** (Address of principal executive offices)	**90024** (Zip Code)

(310) 586-5180
(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 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 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 o

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

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

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

As of November 1, 2013, there were 35,519,409 shares of the registrant s common stock outstanding

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

Boingo Wireless, Inc.

Condensed Consolidated Balance Sheets

(Unaudited)

(In thousands, except per share amounts)

	September 30, 2013	December 31, 2012
Assets		
Current assets:		
Cash and cash equivalents	$ 44,746	$ 58,138
Restricted cash	30	30
Marketable securities	36,493	41,558
Accounts receivable, net	13,034	10,977
Prepaid expenses and other current assets	6,680	2,072
Deferred tax assets	1,199	1,204
Total current assets	102,182	113,979
Property and equipment, net	54,605	42,411
Goodwill	33,045	26,744
Intangible assets, net	15,522	10,594
Deferred tax assets	1,195	4,256
Other assets	3,262	4,548
Total assets	$ 209,811	$ 202,532
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 6,478	$ 4,990
Accrued expenses and other liabilities	11,756	11,019
Deferred revenue	17,908	17,329
Total current liabilities	36,142	33,338
Deferred revenue, net of current portion	24,903	24,123
Other liabilities	1,913	572
Total liabilities	62,958	58,033
Commitments and contingencies (Note 9)		
Stockholders equity:		
Preferred stock, $0.0001 par value; 5,000 shares authorized; no shares issued and outstanding		
Common stock, $0.0001 par value; 100,000 shares authorized; 35,495 and 35,483 shares issued and outstanding at September 30, 2013 and December 31, 2012, respectively	4	4
Additional paid-in capital	184,417	178,219
Accumulated deficit	(38,269)	(34,547)

Total common stockholders equity		146,152		143,676
Non-controlling interests		701		823
Total stockholders equity		146,853		144,499
Total liabilities and stockholders equity	$	209,811	$	202,532

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

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Boingo Wireless, Inc.

Condensed Consolidated Statements of Operations

(Unaudited)

(In thousands, except per share amounts)

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Revenue	$ 28,607	$ 26,017	$ 77,980	$ 74,506
Costs and operating expenses:				
Network access	13,670	10,061	34,375	29,577
Network operations	4,495	3,693	13,199	10,895
Development and technology	2,622	2,300	8,484	7,792
Selling and marketing	3,294	2,567	10,106	7,237
General and administrative	3,201	2,971	11,502	9,455
Amortization of intangible assets	541	296	1,456	778
Total costs and operating expenses	27,823	21,888	79,122	65,734
Income (loss) from operations	784	4,129	(1,142)	8,772
Interest and other (expense) income, net	(2)	33	70	170
Income (loss) before income taxes	782	4,162	(1,072)	8,942
Income tax expense (benefit)	258	1,101	(382)	2,468
Net income (loss)	524	3,061	(690)	6,474
Net income attributable to non-controlling interests	170	284	476	579
Net income (loss) attributable to common stockholders	$ 354	$ 2,777	$ (1,166)	$ 5,895
Net income (loss) per share attributable to common stockholders:				
Basic	$ 0.01	$ 0.08	$ (0.03)	$ 0.17
Diluted	$ 0.01	$ 0.07	$ (0.03)	$ 0.16
Weighted average shares used in computing net income (loss) per share attributable to common stockholders:				
Basic	35,593	35,080	35,620	34,618
Diluted	37,129	37,337	35,620	37,324

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

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Boingo Wireless, Inc.

Condensed Consolidated Statement of Stockholders Equity

(Unaudited)

(In thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated Deficit	Non-controlling Interests	Total Stockholders Equity
Balance at December 31, 2012	35,483	$ 4	$ 178,219	$ (34,547)	$ 823	$ 144,499
Issuance of common stock upon exercise of stock options	374		540			540
Repurchase and retirement of common stock	(362)			(2,556)		(2,556)
Stock-based compensation expense			3,199			3,199
Excess tax benefits from stock-based compensation			2,459			2,459
Non-controlling interests distributions					(598)	(598)
Net (loss) income				(1,166)	476	(690)
Balance at September 30, 2013	35,495	$ 4	$ 184,417	$ (38,269)	$ 701	$ 146,853

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

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Boingo Wireless, Inc.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

	Nine Months Ended September 30, 2013	2012
Cash flows from operating activities		
Net (loss) income	$ (690)	$ 6,474
Adjustments to reconcile net (loss) income including non-controlling interests to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	13,611	11,672
Amortization of intangible assets	1,456	778
Stock-based compensation	3,199	2,163
Excess tax benefits from stock-based compensation	(1,796)	(1,041)
Change in deferred income taxes	5	(420)
Changes in operating assets and liabilities, net of effect of acquisition:		
Accounts receivable	(2,057)	(3,382)
Prepaid expenses and other assets	(296)	1,767
Accounts payable	(509)	(821)
Accrued expenses and other liabilities	(1,695)	(3,552)
Deferred revenue	1,332	3,596
Net cash provided by operating activities	12,560	17,234
Cash flows from investing activities		
Purchases of marketable securities	(33,399)	(52,232)
Proceeds from sales of marketable securities	38,464	15,013
Purchases of property and equipment	(19,150)	(15,755)
Payments for business acquisition, net of cash acquired	(4,874)	(3,185)
Other		(14)
Net cash used in investing activities	(18,959)	(56,173)
Cash flows from financing activities		
Excess tax benefits from stock-based compensation	1,796	1,041
Proceeds from exercise of stock options	540	2,125
Repurchase and retirement of common stock	(2,556)	
Payments of capital leases and notes payable	(96)	(190)
Payments of acquired notes payable and financed liabilities	(6,079)	
Payments to non-controlling interests	(598)	(620)
Net cash (used in) provided by financing activities	(6,993)	2,356
Net decrease in cash and cash equivalents	(13,392)	(36,583)
Cash and cash equivalents at beginning of period	58,138	93,933
Cash and cash equivalents at end of period	$ 44,746	$ 57,350
Supplemental disclosure of cash flow information		
Cash paid for taxes	$ 54	$ 650
Supplemental disclosure of non-cash investing and financing activities		
Property and equipment and software maintenance costs in accounts payable, accrued expenses and other liabilities	4,679	4,129
Assets acquired in business acquisition	17,317	
Liabilities assumed in business acquisition	12,443	

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

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Boingo Wireless, Inc.

Notes to the Condensed Consolidated Financial Statements

(Unaudited)

(In thousands, except shares and per share amounts)

1. The business

Boingo Wireless, Inc. and its subsidiaries (collectively we , us , our or the Company) is a leading global provider of mobile Wi-Fi Internet solutions. Our solutions enable individuals to access our extensive global Wi-Fi network with devices such as smartphones, laptops and tablet computers. Boingo Wireless, Inc. was incorporated on April 16, 2001 in the State of Delaware. We have direct customer relationships with users who have purchased our mobile Internet services, and we provide solutions to our partners which include telecom operators, cable companies, technology companies, enterprise software and services companies, and communications companies to allow their millions of users to connect to the mobile Internet through hotspots in our network.

2. Summary of significant accounting policies

Basis of presentation

The accompanying interim unaudited condensed consolidated financial statements and related notes for the three and nine months ended September 30, 2013 and 2012 are unaudited. The unaudited interim condensed consolidated financial information has been prepared in accordance with the rules and regulations of the SEC for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles (GAAP) in the United States of America (U.S.) for complete financial statements. These financial statements should be read in conjunction with the audited consolidated financial statements and the accompanying notes for the year ended December 31, 2012 contained in our annual report on Form 10-K filed with the SEC on March 18, 2013. The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the annual consolidated financial statements and in the opinion of management, reflects all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of our results of operations for the three and nine months ended September 30, 2013 and 2012, our results of cash flows for the nine months ended September 30, 2013 and 2012, and our financial position as of September 30, 2013. The year-end balance sheet data was derived from audited consolidated financial statements, but does not include all disclosures required by GAAP. Interim results are not necessarily indicative of the results to be expected for an entire year or any other future year or interim period.

During the nine months ended September 30, 2013, the Company recorded certain out-of-period adjustments that decreased net loss attributable to common stockholders by $217. The impact of these out-of-period adjustments is not considered material, individually and in the aggregate, to any of the current or prior quarterly or annual periods.

Principles of consolidation

The unaudited condensed consolidated financial statements include our accounts and our majority owned subsidiaries. We consolidate our 70% ownership of Concourse Communications Detroit, LLC, our 70% ownership of Chicago Concourse Development Group, LLC and our 75% ownership of Boingo Holding Participacoes Ltda. in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 810, *Consolidation*. Other parties interests in consolidated entities are reported as non-controlling interests. All intercompany balances and transactions have been eliminated in consolidation.

Business combinations

The results of businesses acquired in a business combination are included in the Company s condensed consolidated financial statements from the date of the acquisition. Purchase accounting results in assets and liabilities of an acquired business being recorded at their estimated fair values on the acquisition date. Any excess consideration over the fair value of assets acquired and liabilities assumed is recognized as goodwill.

The Company performs valuations of assets acquired and liabilities assumed for an acquisition and allocates the purchase price to its respective net tangible and intangible assets. Determining the fair value of assets acquired and liabilities assumed requires management to use significant judgment and estimates including the selection of valuation methodologies, estimates of future revenues and cash flows, discount rates and selection of comparable companies. The Company engages the assistance of valuation specialists in concluding on fair value measurements in connection with fair values of assets and liabilities assumed in a business combination.

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Transaction costs associated with business combinations are expensed as incurred, and are included in general and administrative expenses in the condensed consolidated statements of operations. There were no significant transaction costs associated with business combinations for the three months ended September 30, 2013. Transaction costs associated with business combinations were $192 for the nine months ended September 30, 2013.

Segment information

We operate as one reportable segment; a service provider of mobile Internet solutions across our managed and operated network and aggregated network for mobile devices such as laptops, smartphones and tablet computers. This single segment is consistent with the internal organization structure and the manner in which operations are reviewed and managed by our Chief Executive Officer, the chief operating decision maker.

Revenue is predominately generated and all significant long-lived tangible assets are held in the U.S. We do not disclose sales by geographic area because to do so would be impracticable. The following is a summary of our revenue by primary revenue source:

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Revenue:				
Retail subscription	$ 8,860	$ 8,621	$ 25,658	$ 24,484
Retail single-use	2,386	3,304	7,802	10,799
Wholesale	14,328	11,631	38,222	34,837
Advertising and other	3,033	2,461	6,298	4,386
Total revenue	$ 28,607	$ 26,017	$ 77,980	$ 74,506

Marketable securities

Our marketable securities consist of available-for-sale securities with original maturities exceeding three months. In accordance with FASB ASC 320, *Investments Debt and Equity Securities,* we have classified securities, which have readily determinable fair values and are highly liquid, as short-term because such securities are expected to be realized within a one-year period. At September 30, 2013 and December 31, 2012, we had $36,493 and $41,558, respectively, in short-term marketable securities and no long-term marketable securities.

Marketable securities are reported at fair value with the related unrealized gains and losses reported as other comprehensive income (loss) until realized or until a determination is made that an other-than-temporary decline in market value has occurred. No significant unrealized gains and losses have been reported during the periods presented. Factors considered by us in assessing whether an other-than-temporary impairment has occurred include the nature of the investment, whether the decline in fair value is attributable to specific adverse conditions affecting the investment, the financial condition of the investee, the severity and the duration of the impairment and whether we have the ability to hold the investment to maturity. When it is determined that an other-than-temporary impairment has occurred, the investment is written down to its market value at the end of the period in which it is determined that an other-than-temporary decline has occurred. The cost of marketable securities sold is based upon the specific identification method. Any realized gains or losses on the sale of investments are reflected as a component of interest and other (expense) income, net.

For the nine months ended September 30, 2013, we had no significant realized or unrealized gains or losses from investments in marketable securities classified as available-for-sale.

Revenue recognition

We generate revenue from several sources including: (i) retail customers under subscription plans for month-to-month network access that automatically renew, and retail single-use access from sales of hourly, daily or other single-use access plans, (ii) platform service arrangements with wholesale customers that provide software licensing, network access, and professional services fees, (iii) wholesale customers that are telecom operators under long-term contracts for access to our distributed antenna system (DAS) at our managed and operated locations, and (iv) display advertisements and sponsorships on our walled garden sign-in pages. Software licensed by our wholesale platform services customers can only be used during the term of the service arrangements and has no utility to them upon termination of the service arrangement.

We recognize revenue when an arrangement exists, services have been rendered, fees are fixed or determinable, no significant obligations remain related to the earned fees and collection of the related receivable is reasonably assured.

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Subscription fees from retail customers are paid monthly in advance and revenue is deferred for the portions of monthly recurring subscription fees collected in advance. We do not have a stated or published refund policy for our Wi-Fi service, although our customer service representatives will provide a refund on a case-by-case basis. These amounts are not significant and are recorded as contra-revenue in the period the refunds are made. Subscription fee revenue is recognized ratably over the subscription period. Revenue generated from retail single-use access is recognized when earned.

Services provided to wholesale partners under platform service arrangements generally contain several elements including: (i) a term license to use our software to access our Wi-Fi network, (ii) access fees for network usage, and (iii) professional services for software integration and customization and to maintain the Wi-Fi service. The term license, monthly minimum network access fees and professional services are billed on a monthly basis based upon predetermined fixed rates. Once the term license for integration and customization are delivered, the fees from the arrangement are recognized ratably over the remaining term of the platform service arrangement. The initial term of platform service license agreements is generally between two to five years and the agreements generally contain renewal clauses. Revenue for network access fees in excess of the monthly minimum amounts is recognized when earned. All elements within existing platform service arrangements are generally delivered and earned concurrently throughout the term of the respective service arrangement.

Revenue generated from access to our DAS networks consists of build-out fees and recurring access fees under certain long-term contracts with telecom operators. Build-out fees paid upfront are generally deferred and recognized ratably over the term of the estimated customer relationship period, once the build-out is complete. Minimum monthly access fees for usage of the DAS networks are non-cancellable and generally escalate on an annual basis. These minimum monthly access fees are recognized ratably over the term of the estimated customer relationship period. The initial term of our contracts with telecom operations and wholesale partners generally range from three to fifteen years and the agreements generally contain renewal clauses. Revenue from network access fees in excess of the monthly minimums is recognized when earned.

In instances where the minimum monthly network access fees escalate over the term of the wholesale service arrangement, an unbilled receivable is recognized when performance is within our control and when we have reasonable assurance that the unbilled receivable balance will be collected.

We adopted the provisions of Accounting Standards Update (ASU) 2009-13, *Revenue Recognition (Topic 605) Multiple-Deliverable Revenue Arrangements* (ASU 2009-13), on a prospective basis on January 1, 2011. For multiple-deliverable arrangements entered into prior to January 1, 2011 that are accounted for under ASC 605-25, *Revenue Recognition Multiple- Deliverable Revenue Arrangements*, we defer recognition of revenue for the full arrangement and recognize all revenue ratably over the wholesale service period for platform service arrangements and the term of the estimated customer relationship period for DAS arrangements, as we do not have evidence of fair value for the undelivered elements in the arrangement. For multiple-deliverable arrangements entered into or materially modified after January 1, 2011 that are accounted for under ASC 605-25, we evaluate whether or not separate units of accounting exist and then allocate the arrangement consideration to all units of accounting based on the relative selling price method using estimated selling prices if vendor specific objective evidence and third party evidence is not available. We recognize the revenue associated with the separate units of accounting upon completion of such services or ratably over the wholesale service period for platform service arrangements and the term of the estimated customer relationship period for DAS arrangements.

Advertising and other revenue is recognized when the services are performed.

Recent accounting pronouncements

In July 2013, the FASB issued ASU 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). This ASU requires the netting of unrecognized tax benefits (UTBs) against a deferred tax asset for a loss or other carryforward that would apply in the settlement of the uncertain tax positions. The UTBs will be netted against all available same-jurisdiction loss or other tax carryforwards that would be utilized, rather than only against carryforwards that are created by the UTBs. ASU 2013-11 will require prospective application with optional retrospective application, and will be effective for reporting periods beginning after December 15, 2013. Early adoption is permitted. The adoption of this standard is not expected to have any impact on our financial statements as we currently present our UTBs as a reduction of our deferred tax assets for a loss or other carryforward rather than as a liability when the uncertain tax position would reduce the loss or other carryforward under the tax law.

In February 2013, the FASB issued ASU 2013-02, *Comprehensive Income Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* (ASU 2013-02). This ASU requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income (AOCI) by component. In addition, an entity is required to present,

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either on the face of the statement where net income (loss) is presented or in the notes, significant amounts reclassified out of AOCI by the respective line items of net income (loss) but only if the amount reclassified is required under GAAP to be reclassified to net income (loss) in its entirety in the same reporting period. For other amounts that are not required under GAAP to be reclassified in their entirety to net income (loss), an entity is required to cross-reference to other disclosures required under GAAP that provide additional detail about those amounts. ASU 2013-02 was effective prospectively for reporting periods beginning after December 15, 2012. We adopted this standard effective January 1, 2013. The adoption of this standard did not have any impact on our financial statements.

3. Acquisition

On February 22, 2013, we acquired all outstanding stock of Endeka Group, Inc. (Endeka). Endeka is a provider of commercial wireless broadband and Internet Protocol television (IPTV) services at certain military bases, as well as Wi-Fi services to certain federal law enforcement training facilities. We acquired Endeka because Endeka s portfolio of venues and management team are natural additions to our managed network business. We have included the operating results of Endeka in our condensed consolidated financial statements since the date of acquisition. The operating results for Endeka for the three and nine months ended September 30, 2013 is not material. The Endeka acquisition is not a significant acquisition for us and actual and pro forma financial statements have therefore not been included.

The acquisition has been accounted for under the acquisition method of accounting in accordance with FASB ASC 805, *Business Combinations*. As such, the assets acquired and liabilities assumed are recorded at their acquisition-date fair values. The total purchase price was $6,623, which includes cash paid at closing, holdback consideration to be paid and additional contingent consideration comprised of two components: (i) a payment (Build Payment) if the amount of the capital expenditures incurred for the substantial completion of a specified build project is less than a target; and (ii) a payment (Milestone Payment) based on revenue generated by certain contracts in fiscal year 2014. There is no maximum to the contingent consideration payments for the Milestone Payment. We do not expect to make any payments associated with the Build Payment and the Milestone Payment will be paid by February 28, 2015.

The fair value of the contingent consideration is based on Level 3 inputs as defined in FASB ASC 820, *Fair Value Measurements and Disclosures*. Further changes in the fair value of the contingent consideration will be recorded through operating income (loss). We allocated the excess of the purchase price over the fair value of assets acquired and liabilities assumed to goodwill, which is not deductible for tax purposes. The goodwill arising from the Endeka acquisition is attributable primarily to expected synergies and other benefits, including the acquired workforce, from combining Endeka with us.

The deferred tax liabilities are provisional pending the filing of Endeka s 2012 and final short period 2013 tax returns. The contingent consideration was valued at the date of acquisition using a discounted cash flow method with probability weighted cash flows and a discount rate of 50.5%. The identifiable intangible assets were primarily valued using the excess earnings, relief from royalty, and replacement cost methods using discount rates ranging from 40.0% to 50.0% and royalty rates ranging from 0.5% to 1.5%, where applicable.

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The amortizable intangible assets are being amortized straight-line over their estimated useful lives. The following summarizes the preliminary purchase price allocation:

		Estimated Fair Value	Estimated Useful Life (years)
Consideration:			
Cash paid	$	4,894	
Holdback consideration		400	
Contingent consideration		1,329	
Total consideration	$	6,623	
Recognized amounts of identifiable assets acquired and liabilities assumed:			
Cash	$	20	
Other current assets		44	
Property and equipment		4,617	
Other assets		12	
Accounts payable		(992)	
Other current liabilities		(186)	
Notes payable and financed liabilities		(6,476)	
Deferred tax liabilities		(3,062)	
Net tangible liabilities acquired		(6,023)	
Existing customer contracts and relationships		4,770	10.0
Technology		930	6.0
Trademark and tradename		300	10.0
Non-compete agreement		250	2.0
Other intangibles		95	10.0
Goodwill		6,301	
Total purchase price	$	6,623	

As of September 30, 2013, we had gross intangible assets of $35,285 and accumulated amortization of $19,763. As of December 31, 2012, we had gross intangible assets of $28,905 and accumulated amortization of $18,311. Based on current intangible assets, amortization expense for the three months ended December 31, 2013 will be $521, and future amortization expense for the years ended December 31, 2014, 2015, 2016, 2017 and 2018 will be $2,034, $1,878, $1,817, $1,651, and $1,444, respectively.

4. Cash and cash equivalents

Cash and cash equivalents consisted of the following:

		September 30, 2013		December 31, 2012
Cash and cash equivalents:				
Cash	$	2,619	$	16,677
Money market accounts		42,127		39,001
Marketable securities				2,460
Total cash and cash equivalents	$	44,746	$	58,138

Marketable securities consist primarily of corporate securities which include commercial paper and corporate debt instruments including notes issued by foreign or domestic corporations which pay in U.S. dollars and carry a rating of A or better with original maturities of three months or less. For the nine months ended September 30, 2013 and 2012, interest income was $145 and $128, respectively, which is included in interest and other (expense) income, net in the accompanying condensed consolidated statements of operations.

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5. Property and equipment

Property and equipment consisted of the following:

	September 30, 2013	December 31, 2012
Leasehold improvements	$ 85,516	$ 72,119
Construction in progress	12,599	6,295
Computer equipment	7,280	7,493
Software	9,848	7,519
Office equipment	413	411
Total property and equipment	115,656	93,837
Less: accumulated depreciation and amortization	(61,051)	(51,426)
Total property and equipment, net	$ 54,605	$ 42,411

Depreciation and amortization of property and equipment is allocated as follows in the accompanying condensed consolidated statements of operations:

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Network access	$ 3,058	$ 2,704	$ 9,140	$ 8,848
Network operations	1,116	687	2,932	2,077
Development and technology	507	375	1,395	656
General and administrative	63	32	144	91
Total depreciation and amortization of property and equipment	$ 4,744	$ 3,798	$ 13,611	$ 11,672

6. Fair value measurement

ASC 820 establishes a three-tiered hierarchy that draws a distinction between market participant assumptions based on (i) quoted prices (unadjusted) in active markets for identical assets and liabilities (Level 1); (ii) inputs other than quoted prices in active markets that are observable either directly or indirectly (Level 2); and (iii) unobservable inputs that require us to use present value and other valuation techniques in the determination of fair value (Level 3). The following table sets forth our financial assets and liabilities that are measured at fair value on a recurring basis:

At September 30, 2013	Level 1	Level 2	Level 3	Total
Assets:				
Cash equivalents	$ 42,127	$	$	$ 42,127
Marketable securities		36,493		36,493

Restricted cash	30			30
Total assets	$ 42,157	$ 36,493	$	$ 78,650
Liabilities:				
Contingent consideration	$	$	$ (1,269)	$ (1,269)
Total liabilities	$	$	$ (1,269)	$ (1,269)

At December 31, 2012	**Level 1**	**Level 2**	**Total**
Assets:			
Cash equivalents	$ 39,001	$ 2,460	$ 41,461
Marketable securities		41,558	41,558
Restricted cash	30		30
Total assets	$ 39,031	$ 44,018	$ 83,049

Our marketable securities utilize Level 2 inputs and consist primarily of corporate securities which include commercial paper and corporate debt instruments including notes issued by foreign or domestic corporations which pay in U.S. dollars and carry a rating of A or better. We have evaluated the various types of securities in our investment portfolio to determine an appropriate fair value hierarchy level based upon trading activity and the observability of market inputs. Due to variations in trading volumes and the lack of quoted market prices in active markets, our fixed maturities are classified as Level 2 securities. The fair value of our fixed maturity marketable securities is derived through the use of a third party pricing source or recent reported trades for identical or similar securities, making adjustments through the reporting date based upon available market observable data.

The Company used the income approach to value the contingent consideration as of September 30, 2013. The contingent consideration used a discounted cash flow method with probability weighted cash flows and a discount rate of 45.0%. The following

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table presents a reconciliation of the beginning and ending amounts related to the fair value of contingent consideration for the Endeka acquisition, categorized as Level 3:

Beginning balance, January 1, 2013	$	
Contingent consideration for acquisition of business		1,329
Change in fair value		(60)
Balance, September 30, 2013	$	1,269

7. Accrued expenses and other liabilities

Accrued expenses and other liabilities consisted of the following:

	September 30, 2013	December 31, 2012
Salaries and wages	$ 2,674	$ 3,312
Revenue share	3,571	3,676
Accrued for construction-in-progress	1,369	1,003
Accrued partner network	1,135	1,134
Deferred rent	883	791
Other	2,124	1,103
Total accrued expenses and other liabilities	$ 11,756	$ 11,019

8. Income taxes

We calculate our interim income tax provision in accordance with ASC 270, *Interim Reporting,* and ASC 740, *Accounting for Income Taxes*. At the end of each interim period, we estimate the annual effective tax rate and apply that rate to our ordinary quarterly earnings. The tax expense or benefit related to significant, unusual, or extraordinary items is recognized in the interim period in which those items occur. In addition, the effect of changes in enacted tax laws, rates, or tax status is recognized in the interim period in which the change occurs.

The computation of the annual estimated effective tax rate at each interim period requires certain estimates and significant judgment, including the expected operating income for the year, projections of the proportion of income earned and taxed in various states, permanent and temporary differences as a result of differences between amounts measured and recognized in accordance with tax laws and financial accounting standards, and the likelihood of recovering deferred tax assets generated in the current year. The accounting estimates used to compute the provision for income taxes may change as new events occur, additional information is obtained, or as the tax environment changes.

During the nine months ended September 30, 2013, we recognized excess windfall tax benefits of $2,459 from stock option exercises. These benefits will decrease income taxes payable for the year ending December 31, 2013, and were recorded as an increase to additional paid-in capital in the accompanying condensed consolidated balance sheet as of September 30, 2013.

Income tax (benefit) expense of $(382) and $2,468 reflects an effective tax rate of 35.6% and 27.6% for the nine months ended September 30, 2013 and 2012, respectively. Our effective tax rate differs from the statutory rate primarily due to benefits from disqualifying dispositions of incentive stock options and adjustments relating to our 2012 and 2011 tax returns for the nine months ended September 30, 2013 and 2012 and non-tax deductible transaction costs related to the acquisition of Endeka for the nine months ended September 30, 2013. Under current tax regulations, we do not receive a tax deduction for the issuance, exercise or disposition of incentive stock options if the employee meets certain holding requirements. If the employee does not meet the holding requirements, a disqualifying disposition occurs, at which time we may receive a tax deduction. We do not record tax benefits related to incentive stock options unless and until a disqualifying disposition is reported. At September 30, 2013, we have net deferred tax assets of $2,394, which includes net operating loss carry-forwards. As of September 30, 2013 and December 31, 2012, we had $392 of uncertain tax positions, $106 of which is a reduction to deferred tax assets, which is presented net of uncertain tax positions, in the accompanying condensed consolidated balance sheets.

We are subject to taxation in the United States and in various states. Our tax years 2010 and forward are subject to examination by the IRS and our tax years 2007 and forward are subject to examination by material state jurisdictions. However, due to prior year loss carryovers, the IRS and state tax authorities may examine any tax years for which the carryovers are used to offset future taxable income.

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9. Commitments and contingencies

Legal proceedings

From time to time, we may be involved in or subject to claims, suits, investigations and proceedings arising out of the normal course of business. We are not a party to any litigation that we believe could have a material adverse effect on our business, financial position, results of operations or cash flows.

10. Stock repurchases

On April 1, 2013, the Company approved a stock repurchase program to repurchase up to $10,000 of the Company s common stock in the open market, exclusive of any commissions, markups or expenses. The stock repurchased will be retired and will resume the status of authorized but unissued shares of common stock. During the three months ended September 30, 2013, we repurchased and retired approximately 207,000 shares under this program for approximately $1,485, excluding commissions paid, at an average price per share of $7.18. During the nine months ended September 30, 2013, we repurchased and retired approximately 362,000 shares under this program for approximately $2,541, excluding commissions paid, at an average price per share of $7.02. As of September 30, 2013, the remaining approved amount for repurchases was approximately $7,459.

11. Stock incentive plans

In March 2011, our board of directors approved the 2011 Equity Incentive Plan (2011 Plan). The 2011 Plan provides for the grant of incentive and nonstatutory stock options, stock appreciation rights, restricted shares of our common stock, stock units, and performance cash awards. As of January 1 of each year, the number of shares of common stock reserved for issuance under our stock incentive plan shall automatically be increased by a number equal to the lesser of (a) 4.5% of the total number of shares of common stock then outstanding, (b) 3,000,000 shares of common stock and (c) as determined by our board of directors. As of September 30, 2013, 7,108,013 shares of common stock are reserved for issuance.

No further awards will be made under our Amended and Restated 2001 Stock Incentive Plan (2001 Plan), and it will be terminated. Options outstanding under the 2001 Plan will continue to be governed by their existing terms.

We recognized stock-based compensation expense as follows:

	Three Months Ended September 30,	Nine Months Ended September 30,

	2013	2012	2013	2012
Network operations	$ 241	$ 117	$ 638	$ 227