GLOWPOINT INC
Form 10-Q
November 10, 2009

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

x Quarterly report under Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended September 30, 2009.
or

o Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number: 0-25940

GLOWPOINT, INC.
(Exact Name of registrant as Specified in its Charter)

Delaware (State or other Jurisdiction of Incorporation or Organization)	77-0312442 (I.R.S. Employer Number)

225 Long Avenue, Hillside, New Jersey 07205
(Address of Principal Executive Offices)

312-235-3888
(Issuer'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 o 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 definition of "accelerated filer", "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one)

Large accelerated filer	o	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	x

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

The number of shares outstanding of the registrant's common stock as of November 10, 2009 was 64,989,462.

GLOWPOINT, INC

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* The Condensed Consolidated Balance Sheet at December 31, 2008 has been derived from the audited consolidated financial statements filed as an exhibit to our Report on Form 10-K on March 31, 2009.

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GLOWPOINT, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except par value and shares)

	September 30, 2009 (Unaudited)	December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,124	$ 1,227
Accounts receivable, net of allowance for doubtful accounts of $260 and $301, respectively	2,895	3,090
Prepaid expenses and other current assets	403	294
Total current assets	4,422	4,611
Property and equipment, net	2,739	2,533
Other assets	31	33
Total assets	$ 7,192	$ 7,177
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Accounts payable	$ 2,855	$ 2,367
Accrued expenses	989	842
Accrued sales taxes and regulatory fees	4,088	4,535
Customer deposits	472	606
Deferred revenue	257	325
Current portion of capital lease	116	161
Total current liabilities	8,777	8,836
Long term liabilities:		
Senior Secured Notes, net of discount of $240	—	1,482
Capital lease, less current portion	—	72
Total long term liabilities	—	1,554
Total liabilities	8,777	10,390
Commitments and contingencies		
Stockholders' deficit:		
Preferred stock, $.0001 par value 7,500 shares authorized and convertible; and 4,509 and 3,790 shares issued and outstanding recorded at fair value, respectively (liquidation value of $33,815 and $28,423, respectively) (see Note 14 for information related to Insider Purchasers – related parties)	14,275	11,574
Common stock, $.0001 par value;150,000,000 shares authorized; 66,542,353 and 48,374,954 shares issued; 64,977,462 and 46,810,063 shares outstanding, respectively	7	5
Additional paid-in capital	150,532	172,000
Accumulated deficit	(165,016)	(185,409)
	(202)	(1,830)
Less: Treasury stock, 1,564,891 shares at cost	(1,383)	(1,383)
Total stockholders' deficit	(1,585)	(3,213)
Total liabilities and stockholders' deficit	$ 7,192	$ 7,177

See accompanying notes to condensed consolidated financial statements.

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GLOWPOINT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008
Revenue	$19,928	$18,557	$6,541	$6,066
Cost of revenue	10,157	10,757	3,321	3,630
Gross margin	9,771	7,800	3,220	2,436
Operating expenses:				
Sales and marketing	2,656	2,717	791	811
General and administrative	7,898	6,565	2,291	2,269
Total operating expense	10,554	9,282	3,082	3,080
Income (loss) from operations	(783)	(1,482)	138	(644)
Interest and other expense (income):				
Interest expense, including $0, $111, $0 and $44, respectively, for Insider Purchasers	273	3,425	60	1,293
Loss on extinguishment of debt	254	—	—	—
Interest income	—	(19)	—	(3)
Increase (decrease) in fair value of derivative financial instruments	1,848	(153)	1,157	(211)
Amortization of deferred financing costs, including $37 and $13, respectively, for Insider Purchasers	—	368	—	130
Total interest and other expense, net	2,375	3,621	1,217	1,209
Net loss	(3,158)	(5,103)	(1,079)	(1,853)
Gain (loss) on redemption of preferred stock	(64)	—	1,935	—
Net income (loss) attributable to common stockholders	$(3,222)	$(5,103)	$856	$(1,853)
Net income (loss) attributable to common stockholders per share:				
Basic	$(0.07)	$(0.11)	$0.02	$(0.04)
Diluted	$(0.07)	$(0.11)	$0.01	$(0.04)
Weighted average number of common shares:				
Basic	49,273	45,440	55,861	45,590
Diluted	49,273	45,440	102,901	45,590

See accompanying notes to condensed consolidated financial statements.

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GLOWPOINT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' DEFICIT
Nine Months Ended September 30, 2009
(In thousands)
(Unaudited)

	Common Stock		Additional Paid In	Accumulated	Series A-2 (Note A) Preferred Stock		Treasury Stock		
	Shares	Amount	Capital	Deficit	Shares	Amount	Shares	Amount	Total
Balance at January 1, 2009	48,375	$ 5	$ 172,000	$ (185,409)	4	$ 11,574	1,565	$ (1,383)	$ (3,213)
Cumulative effect of reclassification of warrants (ASC Topic 815)	—	—	(26,173)	23,551	—	—	—	—	(2,622)
Balance at January 1, 2009, as adjusted	48,375	5	145,827	(161,858)	4	11,574	1,565	(1,383)	(5,835)
Net loss	—	—	—	(3,158)	—	—	—	—	(3,158)
Stock-based compensation - stock options	—	—	213	—	—	—	—	—	213
Stock-based compensation - restricted stock	775	—	225	—	—	—	—	—	225
August 2009 Warrant Exchange	17,372	2	(2)	—	—	—	—	—	—
Exercise of stock options	20	—	8	—	—	—	—	—	8
Series A-1 Preferred Stock issued in connection with the 2009 Private Placement	—	—	—	—	1	2,637	—	—	2,637
Elimination of derivative liabilities	—	—	4,751	—	—	—	—	—	4,751
Loss on redemption of Series A Preferred Stock	—	—	(1,999)	—	—	1,999	—	—	—
Gain on redemption of Series A-1 Preferred Stock	—	—	1,935	—	—	(1,935)	—	—	—
Costs related to 2009 Private Placement, warrant and Preferred Stock exchange	—	—	(426)	—	—	—	—	—	(426)
Balance at September 30, 2009	66,542	$ 7	$ 150,532	$ (165,016)	5	$ 14,275	1,565	$ (1,383)	$ (1,585)

Note A – In March 2009 the shares of Series A Preferred Stock outstanding at December 31, 2008 were exchanged for an equal number of shares of newly-created Series A-1 Convertible Preferred Stock ("Series A-1 Preferred Stock"). In

August 2009 the shares of Series A-1 Preferred Stock then outstanding were exchanged for an equal number of shares of newly-created Series A-2 Convertible Preferred Stock (“Series A-2 Preferred Stock”)

See accompanying notes to condensed consolidated financial statements.

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GLOWPOINT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008
Cash flows from Operating Activities:		
Net loss	$ (3,158)	$ (5,103)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	790	959
Other expense recognized for the increase in the estimated fair value of the derivative financial instruments	1,848	(153)
Amortization of deferred financing costs	—	368
Bad debt expense	191	85
Accretion of discount on Senior Secured Notes	23	2,158
Loss on disposal of equipment	8	17
Loss on extinguishment of debt	254	—
Stock-based compensation	438	436
Increase (decrease) attributable to changes in assets and liabilities:		
Accounts receivable	4	(442)
Prepaid expenses and other current assets	(109)	(18)
Other assets	2	3
Accounts payable	488	1,293
Customer deposits	(134)	(114)
Accrued expenses, sales taxes and regulatory fees	(232)	842
Deferred revenue	(68)	10
Net cash provided by operating activities	345	341
Cash flows from Investing Activities:		
Purchases of property and equipment	(1,004)	(847)
Net cash used in investing activities	(1,004)	(847)
Cash flows from Financing Activities:		
Proceeds from preferred stock offering	1,800	—
Proceeds from exercise of stock options	8	—
Principal payments for capital lease	(118)	(91)
Purchase of Senior Secured Notes	(750)	—
Costs related to private placement	(384)	—
Net cash provided by (used in) financing activities	556	(91)
Decrease in cash and cash equivalents	(103)	(597)
Cash and cash equivalents at beginning of period	1,227	2,312
Cash and cash equivalents at end of period	$ 1,124	$ 1,715
Supplement disclosures of cash flow information:		
Cash paid during the period for		

Interest	$	108	$	91
Non-cash investing and financing activities:				
Exchange of Senior Secured Notes for Series A-1 Preferred Stock	$	1,076	$	—
Additional Senior Secured Notes issued as payment for interest		55		1,020
Costs related to private placement incurred by issuance of placement agent warrants		42		—
Settlement of accrued 2007 management bonus with restricted stock		—		179

See accompanying notes to condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2009
(Unaudited)

Note 1 - Basis of Presentation

The Business

Glowpoint, Inc. ("Glowpoint" or "we" or "us" or the "Company"), a Delaware corporation, is a leading provider of advanced video communications solutions. Our suite of advanced and robust telepresence and video communications solutions enable organizations to communicate with each other over disparate networks and technology platforms – empowering business, governmental agencies and educational institutions to sharply boost the impact and productivity of their internal and external communications while at the same time reducing their on-going operating costs. We support thousands of video communications systems in over 35 countries with our 24/7 managed video services, powering Fortune® 500 companies, major broadcasters, as well as global carriers and video equipment manufacturers and their customers around the world. The Company operates in one segment and therefore segment information is not presented.

We view our services as analogous to cellular service providers in the cellular telephone industry. Regardless of the cellular phone purchased, users must select a cellular service provider to make it work. Users make that service decision based on the features, reliability and price offered by the service provider. In our industry, regardless of the video conferencing or telepresence equipment purchased, or the network connecting it, Glowpoint provides the managed services to make it work. In doing so, we offer a vast array of video communications solutions, including video application services, video operations services (VNOC) for telepresence, managed network services, IP and ISDN videoconferencing services, multi-point conferencing (bridging), technology hosting and management, and professional services. We provide these services to a wide variety of companies, from large enterprises and governmental entities to small and medium-sized businesses. Glowpoint is primarily focused on high quality two-way video communications. With the advent of HD (High Definition) and telepresence solutions, we combined various components of our features and services, and developed new ones, to create a comprehensive service offering for enterprises and their end users that can support any of the telepresence products on the market today. Glowpoint also wholesales these services and provides private-labeled branding for manufacturers, carriers, and integrators seeking to offer this service as a value-add to their offerings for their customer bases.

Glowpoint's video communications solutions involve two major components, the Glowpoint managed video applications services and the Glowpoint managed network services. Glowpoint has focused its sales and marketing efforts on the managed video application services, which are network agnostic and may be leveraged by customers on any QoS (Quality of Service) network that supports two-way video transport. Glowpoint's services for telepresence are in increased demand because they address the need for a single point of contact to provide monitoring, scheduling, support, and management of telepresence rooms and the associated equipment. Additionally, companies look to Glowpoint as a resource to provide secure business-to-business (B2B) support when using the video systems to communicate beyond their internal enterprise use. Our Telepresence inter-Exchange Network (TEN) is a suite of services and applications designed to overcome the challenges of using video outside of a company's private network, such as interconnectivity and interoperability, and we believe will be a critical component for enhanced B2B video communications. Our managed video application services are sold as a monthly subscription service and may also include Glowpoint managed network services as an option.

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Liquidity and Going Concern

Our condensed consolidated financial statements have been prepared assuming that we will continue as a going concern. We have incurred recurring operating losses and negative operating cash flows since our inception including a net loss attributable to common stockholders of $3,222,000 for the nine months ended September 30, 2009. At September 30, 2009, we had cash and cash equivalents of $1,124,000, a working capital deficit of $4,355,000 and an accumulated deficit of $165,016,000. We have raised capital in private placements and have amended the terms of our Preferred Stock to eliminate any dividends until January 2013, but continue to sustain losses and negative operating cash flows. Additionally, current economic conditions may cause a decline in business and consumer spending which could adversely affect our business and financial performance. These factors raise substantial doubt as to our ability to continue as a going concern. Assuming we are able to negotiate favorable terms with the authorities regarding our sales and use taxes and we are not adversely affected by the current economic conditions, we believe that our available capital as of September 30, 2009 will enable us to continue as a going concern through September 30, 2010. There are no assurances that we will be able to raise additional capital as needed upon acceptable terms, nor that the current economic conditions will not negatively impact us. If the current economic conditions negatively impact us and/or we are unable to raise additional capital as needed upon acceptable terms, it would have a material adverse effect on the Company. The accompanying consolidated financial statements do not include any adjustments that might result from this uncertainty.

Quarterly Financial Information and Results of Operations

The condensed consolidated financial statements as of September 30, 2009 and for the nine and three months ended September 30, 2009 and 2008 are unaudited and, in the opinion of management, include all adjustments (consisting only of normal recurring adjustments) necessary to present fairly the financial position as of September 30, 2009, and the results of operations for the nine and three months ended September 30, 2009 and 2008 and cash flows for the nine months ended September 30, 2009 and 2008. The results for the nine and three months ended September 30, 2009 are not necessarily indicative of the results to be expected for the entire year. While management of the Company believes that the disclosures presented are adequate to make the information not misleading, these condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the footnotes thereto for the fiscal year ended December 31, 2008 as filed with the Securities and Exchange Commission as an exhibit to our Form 10-K on March 31, 2009 (the "Audited 2008 Financials").

See "Note 2 - Basis of Presentation, Liquidity and Summary of Significant Accounting Policies" in the Audited 2008 Financials for a discussion of the estimates and judgments inherent in the Company's accounting for allowance for doubtful accounts, concentration of credit risk, lives of property and equipment, income taxes, stock-based compensation and accrued sales taxes and regulatory fees. There have been no changes to our critical accounting policies in the nine months ended September 30, 2009. Critical accounting policies and the significant estimates made in accordance with them are regularly discussed with our Audit Committee.

Note 2 – Summary of Significant Accounting Policies

Principles of Consolidation

The condensed consolidated financial statements include the accounts of Glowpoint and our wholly owned subsidiary, GP Communications, LLC. All material inter-company balances and transactions have been eliminated in consolidation.

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Reclassifications

Certain prior year amounts have been reclassified to conform to the current period presentation.

Use of Estimates

Preparation of the condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts could differ from the estimates made. We continually evaluate estimates used in the preparation of the condensed consolidated financial statements for reasonableness. Appropriate adjustments, if any, to the estimates used are made prospectively based upon such periodic evaluation. The significant areas of estimation include determining the allowance for doubtful accounts, deferred tax valuation allowance, accrued sales taxes, the estimated life of customer relationships, the fair value of derivative financial instruments and the estimated lives and recoverability of property and equipment.

Financial Instruments

The Company considers its cash and cash equivalents, accounts receivable, accounts payable, and derivative instruments to meet the definition of financial instruments. The carrying amount of cash and cash equivalents, accounts receivable and accounts payable approximated their fair value due to the short maturities of these instruments. See Note 12 for additional discussion.

Accounting Standards Updates

In June 2009, the Financial Accounting Standards Board (“FASB”) issued its final Statement of Financial Accounting Standards (“SFAS)” No. 168 – “The FASB Accounting Standards ASC Topic and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162”. (“SFAS No. 168”). SFAS No. 168 made the FASB Accounting Standards Codification (the “ASC”) the single source of U.S. Generally Accepted Accounting Policies (“U.S. GAAP”) used by nongovernmental entities in the preparation of financial statements, except for rules and interpretive releases of the SEC under authority of federal securities laws, which are sources of authoritative accounting guidance for SEC registrants. The ASC is meant to simplify user access to all authoritative accounting guidance by reorganizing U.S. GAAP pronouncements into roughly 90 accounting topics within a consistent structure; its purpose is not to create new accounting and reporting guidance. The ASC supersedes all existing non-SEC accounting and reporting standards and was effective for the Company beginning July 1, 2009. Following SFAS No. 168, the Board will not issue new standards in the form of Statements, FASB Staff Positions, or Emerging Issues Task Force Abstracts; instead, it will issue Accounting Standards Updates. The FASB will not consider Accounting Standards Updates as authoritative in their own right; these updates will serve only to update the ASC topic, provide background information about the guidance, and provide the bases for conclusions on the change(s) in the ASC. In the description of ASC and Accounting Standards Updates (“ASU”) that follows, references in “italics” relate to ASC or ASU topics, and their descriptive titles, as appropriate.

In April 2009, the FASB updated ASC topic 825, “Financial Instruments” (“ASC Topic 825”) which requires disclosures about fair value of financial instruments for interim reporting periods as well as in annual financial statements. The Company has adopted the amended provisions of ASC Topic 825 effective June 30, 2009 and has included the required disclosures in Note 12.

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In May 2008, the FASB updated ASC topic 470, “Debt – Debt with Conversion and Other Options” (“ASC Topic 470”) which clarifies the accounting treatment of convertible debt instruments Additionally, ASC Topic 470 specifies that issuers of such instruments should separately account for the liability and equity components in a manner that will reflect the entity’s nonconvertible debt borrowing rate when interest cost is recognized in subsequent periods. ASC Topic 470 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. We adopted the amended sections of ASC Topic 470 beginning in the first quarter of 2009, and this standard must be applied on a retrospective basis. The adoption of ASC Topic 470 did not have a material impact on the Company’s consolidated results of operations and financial condition.

In May 2009, the FASB updated ASC topic 855 “Subsequent Events” (“ASC Topic 855”), which is effective for reporting periods ending after June 15, 2009. ASC Topic 855 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date, but before financial statements are issued, or are available to be issued. The Company adopted the amended sections of ASC Topic 855 and it did not have an impact on the Company’s consolidated financial statements. The Company evaluated all events or transactions that occurred after September 30, 2009 up through November 10, 2009. During this period no material subsequent events came to our attention.

In September 2009, the FASB issued ASU 2009-14, “Certain Revenue Arrangements That Include Software Elements” (“ASU 2009-14”), which excludes tangible products containing software components and non-software components that function together to deliver the product’s essential functionality from the scope of Subtopic 985-605, “Revenue Recognition.” ASU 2009-14 is effective for periods beginning after December 15, 2009 with earlier adoption permitted. The Company is currently evaluating the timing of its adoption of ASU 2009-14 and the impact that ASU 2009-14 will have on its consolidated financial statements.

In October 2009, the FASB issued ASU 2009-13 which supersedes certain guidance in ASC 605-25, “Revenue Recognition — Multiple Element Arrangements”. This topic requires an entity to allocate arrangement consideration at the inception of an arrangement to all of its deliverables based on their relative selling prices. This topic is effective for annual reporting periods beginning after June 15, 2010. The Company is currently evaluating the impact that this topic will have on its consolidated financial statements.

Derivative Financial Instruments

The Company’s objectives in using debt-related derivative financial instruments are to obtain the lowest cash cost source of funds within a targeted range of variable-to fixed-rate debt obligations. Derivatives are recognized in the consolidated balance sheets at fair value as required by ASC topic 815“Derivatives and Hedging” (“ASC Topic 815”). The estimated fair value of the derivative liabilities is calculated using the Black-Scholes method where applicable and such estimates are revalued at each balance sheet date, with changes in value recorded as other income or expense in the consolidated statement of operations. As a result of the Company’s adoption of ASC Topic 815, effective January 1, 2009 all warrants were accounted for as derivatives. See Note 11.

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As part of the August 2009 Warrant and Preferred Stock Exchange (see Note 4), all 40,912,000 of the warrants to acquire shares of common stock with an exercise price of $0.40 (the “$0.40 Warrants”) were amended to require the consent of a majority of the warrant holders in order to consummate a financing at a price per share of common stock below $0.40, thereby eliminating the provisions that protect holders from a decline in the stock price (or “Down-round” provisions) and the need to account for a derivative liability for these warrants. Concurrently 39,088,000 of the $0.40 Warrants were exchanged for common stock and the remaining 1,824,000 $0.40 Warrants are outstanding until November 2013. The accrued derivative liability of $4,751,000, which was related to the $0.40 Warrants, was then transferred to Paid In Capital. The 1,640,000 warrants which expire in March 2010 still have Down-round provisions but the derivative liability was immaterial at September 30, 2009.

Revenue Recognition

We recognize subscription revenue when the related services have been performed. Revenue billed in advance is deferred until the revenue has been earned. Other service revenue, including amounts related to surcharges charged by our carriers, related to the Glowpoint managed network service and the multi-point video and audio bridging services are recognized as service is provided. As the non-refundable, upfront activation fees charged to the subscribers do not meet the criteria as a separate unit of accounting, they are deferred and recognized over the twelve to twenty-four month period estimated life of the customer relationship. Revenue related to integration services is recognized at the time the services are performed, and presented as required by ASC topic 605 “Revenue Recognition”. Revenues derived from other sources are recognized when services are provided or events occur.

Long-Lived Assets

We evaluate impairment losses on long-lived assets used in operations, primarily fixed assets, when events and circumstances indicate that the carrying value of the assets might not be recoverable as required by ASC topic 360 “Property, Plant and Equipment”. For purposes of evaluating the recoverability of long-lived assets, the undiscounted cash flows estimated to be generated by those assets are compared to the carrying amounts of those assets. If and when the carrying values of the assets exceed their fair values, the related assets will be written down to fair value. In the nine and three months ended September 30, 2009 and 2008, no impairment indicators were noted or impairment losses recorded.

Related Party Transactions

The Company provides video services to a company in which one of our directors is an officer (the “Video Services”). The Company receives consulting and tax services from an accounting firm in which one of our prior directors, who resigned in May 2009, is a partner and software development from a firm in which one of our prior directors, who resigned in March 2009, is the president. Management believes that such transactions are at arm’s-length and for terms that would have been obtained from unaffiliated third parties. The fees incurred for consulting and tax services and software development (the “Consulting Services”) are only included for the period that the partner of the accounting firm and company’s president were directors of the Company. The Company continues to utilize these firms for Consulting Services.

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Consulting Services and Video Services are as follows for the nine and three months ended September 30, 2009 and 2008 (in thousands):

	Nine Months Ended September 30,		Three Months Ended September 30,		
	2009	2008	2009	2008	
Consulting Services	$26	$153	$—	$72	&#