

SALESFORCE COM INC
Form 10-Q
May 26, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended April 30, 2011

OR

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

salesforce.com, inc.

(Exact name of registrant as specified in its charter)

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Delaware
(State or other jurisdiction of
incorporation or organization)

94-3320693
(IRS Employer
Identification No.)

The Landmark @ One Market, Suite 300

San Francisco, California 94105

(Address of principal executive offices)

Telephone Number (415) 901-7000

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

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

As of April 30, 2011, there were approximately 133.9 million shares of the Registrant's Common Stock outstanding.

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Condensed Consolidated Balance Sheets

(in thousands)

	April 30, 2011 (unaudited)	January 31, 2011
Assets		
Current assets:		
Cash and cash equivalents	\$ 664,612	\$ 424,292
Marketable securities	99,224	72,678
Accounts receivable, net	270,816	426,943
Deferred commissions	65,800	67,774
Deferred income taxes	23,791	27,516
Prepaid expenses and other current assets	63,886	55,721
Total current assets	1,188,129	1,074,924
Marketable securities, noncurrent	758,449	910,587
Property and equipment, net	446,268	387,174
Deferred commissions, noncurrent	46,645	48,842
Deferred income taxes, noncurrent	47,432	41,199
Capitalized software, net	124,661	127,987
Goodwill	406,889	396,081
Other assets, net	109,595	104,371
Total assets	\$ 3,128,068	\$ 3,091,165
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 16,969	\$ 18,106
Accrued expenses and other current liabilities	295,970	345,121
Deferred revenue	893,904	913,239
Convertible senior notes, net (Note 2)	478,369	0
Total current liabilities	1,685,212	1,276,466
Convertible senior notes, net	0	472,538
Income taxes payable, noncurrent	20,292	18,481
Long-term lease liabilities and other	49,062	25,487
Deferred revenue, noncurrent	21,229	21,702
Total liabilities	1,775,795	1,814,674
Temporary equity (Note 2)	96,631	0
Stockholders' equity:		
Common stock	134	133
Additional paid-in capital	1,083,867	1,098,604
Accumulated other comprehensive income	76	6,719
Retained earnings	171,565	171,035
Total stockholders' equity	1,255,642	1,276,491

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Total liabilities, temporary equity and stockholders' equity	\$ 3,128,068	\$ 3,091,165
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See accompanying Notes.

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Condensed Consolidated Statements of Operations

(in thousands, except per share data)

(unaudited)

	Three months ended April 30,	
	2011	2010
Revenues:		
Subscription and support	\$ 473,504	\$ 350,712
Professional services and other	30,860	26,101
Total revenues	504,364	376,813
Cost of revenues (1):		
Subscription and support	75,243	44,057
Professional services and other	27,823	27,524
Total cost of revenues	103,066	71,581
Gross profit	401,298	305,232
Operating expenses (1):		
Research and development	65,292	40,122
Marketing and sales	254,471	175,867
General and administrative	84,338	56,193
Total operating expenses	404,101	272,182
Income (loss) from operations	(2,803)	33,050
Investment income	8,055	7,875
Interest expense	(3,671)	(7,060)
Other expense	(800)	(1,973)
Income before provision for income taxes and noncontrolling interest	781	31,892
Provision for income taxes	(251)	(12,016)
Consolidated net income	530	19,876
Less: Net income attributable to noncontrolling interest	0	(2,131)
Net income attributable to salesforce.com	\$ 530	\$ 17,745
Basic net income per share attributable to salesforce.com common shareholders	\$ 0.00	\$ 0.14
Diluted net income per share attributable to salesforce.com common shareholders	\$ 0.00	\$ 0.13
Shares used in computing basic net income per share	133,454	128,032
Shares used in computing diluted net income per share	141,062	132,251

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

Cost of revenues	\$ 3,651	\$ 3,074
Research and development	7,839	4,102
Marketing and sales	23,787	12,210

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General and administrative

See accompanying Notes.

12,281

7,082

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Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	Three months ended April 30,	
	2011	2010
Operating activities		
Consolidated net income	\$ 530	\$ 19,876
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	29,593	14,505
Amortization of debt discount and transaction costs	2,255	5,451
Amortization deferred commissions	24,675	19,489
Expenses related to stock-based awards	47,558	26,468
Excess tax benefits from employee stock plans	(2,034)	(9,288)
Changes in assets and liabilities:		
Accounts receivable, net	156,127	138,951
Deferred commissions	(20,504)	(19,308)
Prepaid expenses and other current assets	(9,383)	9,939
Other assets	(2,713)	(1,439)
Accounts payable	(1,137)	(1,658)
Accrued expenses and other current liabilities	(65,641)	(19,984)
Deferred revenue	(19,808)	(39,819)
Net cash provided by operating activities	139,518	143,183
Investing activities		
Business combinations, net of cash acquired	(13,335)	0
Land activity and building improvements	(1,014)	0
Strategic investments	(5,433)	(500)
Purchase of marketable securities	(232,127)	(816,358)
Sales of marketable securities	352,070	204,153
Maturities of marketable securities	6,515	116,262
Capital expenditures	(27,314)	(11,690)
Net cash provided by (used in) investing activities	79,362	(508,133)
Financing activities		
Purchase of subsidiary stock	0	(1,273)
Proceeds from the exercise of stock options	32,286	37,516
Excess tax benefits from employee stock plans	2,034	9,288
Contingent consideration payment related to prior business combination	(2,800)	0
Principal payments on capital lease obligations	(3,562)	(1,918)
Net cash provided by financing activities	27,958	43,613
Effect of exchange rate changes	(6,518)	825
Net increase (decrease) in cash and cash equivalents	240,320	(320,512)
Cash and cash equivalents, beginning of period	424,292	1,011,306

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Cash and cash equivalents, end of period	\$ 664,612	\$ 690,794
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Supplemental cash flow disclosure:

Cash paid (received) during the period for:

Interest, net	\$ 337	\$ 215
Income taxes, net of tax refunds	\$ 10,978	\$ (5,513)

Non-cash financing and investing activities:

Fixed assets acquired under capital leases	\$ 47,203	\$ 431
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See accompanying Notes.

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Notes to Condensed Consolidated Financial Statements

1. Summary of Business and Significant Accounting Policies

Description of Business

Salesforce.com, inc. (the Company) is a leading provider of enterprise cloud computing applications. The Company provides a comprehensive customer and collaboration relationship management (CRM) service to businesses of all sizes and industries worldwide and provides a technology platform for customers and developers to build and run applications. The Company offers its enterprise cloud computing services on a subscription basis.

Fiscal Year

The Company's fiscal year ends on January 31. References to fiscal 2012, for example, refer to the fiscal year ending January 31, 2012.

Basis of Presentation

The accompanying condensed consolidated balance sheet as of April 30, 2011 and the condensed consolidated statements of operations and the condensed consolidated statements of cash flows for the three months ended April 30, 2011 and 2010, respectively, are unaudited. The condensed consolidated balance sheet data as of January 31, 2011 was derived from the audited consolidated financial statements which are included in the Company's Form 10-K for the fiscal year ended January 31, 2011, which was filed with the Securities and Exchange Commission (the SEC) on March 23, 2011. The accompanying statements should be read in conjunction with the audited consolidated financial statements and related notes contained in the Company's fiscal 2011 Form 10-K.

The accompanying condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) for interim financial information. Accordingly, they do not include all of the financial information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of the Company's management, the unaudited condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements in the Form 10-K, and include all adjustments necessary for the fair presentation of the Company's statement of financial position as of April 30, 2011, and its results of operations and its cash flows for the three months ended April 30, 2011 and 2010. All adjustments are of a normal recurring nature. The results for the three months ended April 30, 2011 are not necessarily indicative of the results to be expected for any subsequent quarter or for the fiscal year ending January 31, 2012.

On February 1, 2011, the Company adopted on a prospective basis Accounting Standards Update No. 2009-13, *Revenue Recognition (Topic 605) Multiple-Deliverable Revenue Arrangements* (ASU 2009-13). As a result of the adoption of ASU 2009-13, the Company has updated its accounting policy for revenue recognition related to multiple-deliverable arrangements.

Use of Estimates

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

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

the best estimate of selling price of the deliverables included in multiple-deliverable revenue arrangements,

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Notes to Condensed Consolidated Financial Statements (Continued)

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

recognition and measurement of current and deferred income taxes,

the fair value of stock awards issued, and

the valuation of strategic investments and the determination of other-than-temporary impairments.

Actual results could differ materially from those estimates.

Principles of Consolidation

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

Segments

The Company operates in one reportable segment. Operating segments are defined as components of an enterprise about which separate financial information is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and assessing performance. Since the Company operates in one operating segment, all required financial segment information can be found in the consolidated financial statements.

Foreign Currency Translation

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

Concentrations of Credit Risk and Significant Customers

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

No customer accounted for more than five percent of accounts receivable at April 30, 2011 and 2010. No single customer accounted for five percent or more of total revenue in the three months ended April 30, 2011 and 2010.

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Notes to Condensed Consolidated Financial Statements (Continued)

As of April 30, 2011 and January 31, 2011, assets located outside the Americas were 16 percent and 16 percent of total assets, respectively.

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

	Three months ended April 30,	
	2011	2010
Revenues by geography:		
Americas	\$ 340,018	\$ 259,284
Europe	94,395	66,842
Asia Pacific	69,951	50,687
	\$ 504,364	\$ 376,813

Cash and Cash Equivalents

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

Marketable Securities

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

Fair Value Measurement

The Company reports its financial and non-financial assets and liabilities that are re-measured and reported at fair value at each reporting period. The Company uses a three-tier fair value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

- Level 1.** Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2.** Include other inputs that are directly or indirectly observable in the marketplace.
- Level 3.** Unobservable inputs which are supported by little or no market activity.

All of the Company's cash equivalents, marketable securities and foreign currency derivative contracts are classified within Level 1 or Level 2 because the Company's cash equivalents, marketable securities and foreign currency derivative contracts are valued using quoted market prices or alternative pricing sources and models utilizing market observable inputs. The Company's contingent considerations related to acquisitions are classified within Level 3 because the liabilities are valued using significant unobservable inputs.

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Notes to Condensed Consolidated Financial Statements (Continued)

The following table presents information about the Company's assets and liabilities that are measured at fair value as of April 30, 2011 and indicates the fair value hierarchy of the valuation (in thousands):

Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balances as of April 30, 2011
Cash equivalents (1):				
Time deposits	\$ 27,775	\$ 0	\$ 0	\$ 27,775
Money market mutual funds	84,006	0	0	84,006
Marketable securities:				
Corporate notes and obligations	0	602,696	0	602,696
U.S. agency obligations	0	67,156	0	67,156
U.S. treasury securities	26,838	0	0	26,838
Government obligations	6,537	0	0	6,537
Mortgage backed securities	0	36,684	0	36,684
Collateralized mortgage obligations	0	92,602	0	92,602
Municipal securities	0	25,160	0	25,160
Foreign currency derivative contracts (2)	0	407	0	407
Total Assets	\$ 145,156	\$ 824,705	\$ 0	\$ 969,861
Liabilities				
Foreign currency derivative contracts (3)	\$ 0	\$ 4,673	\$ 0	\$ 4,673
Contingent consideration (related to acquisitions, see Note 4) (3)	0	0	14,400	14,400
Total Liabilities	\$ 0	\$ 4,673	\$ 14,400	\$ 19,073

- (1) Included in cash and cash equivalents in the accompanying Condensed Consolidated Balance Sheet as of April 30, 2011, in addition to \$552.8 million of cash.
- (2) Included in prepaid expenses and other current assets in the accompanying Condensed Consolidated Balance Sheet as of April 30, 2011.
- (3) Included in accrued expenses and other current liabilities in the accompanying Condensed Consolidated Balance Sheet as of April 30, 2011.

The following table presents the Company's only liability measured at fair value using significant unobservable inputs (Level 3) at April 30, 2011. This liability consists of the Company's contingent considerations related to acquisitions and the fair value was determined using a discounted cash flow model (in thousands):

Balance at February 1, 2011	\$ 17,138
Additions	262
Payments	(3,000)
Balance at April 30, 2011	\$ 14,400

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Notes to Condensed Consolidated Financial Statements (Continued)

The following table presents information about the Company's assets and liabilities that are measured at fair value as of January 31, 2011 and indicates the fair value hierarchy of the valuation (in thousands):

Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balances as of January 31, 2011
Cash equivalents (1):				
Time deposits	\$ 26,565	\$ 0	\$ 0	\$ 26,565
Money market mutual funds	122,516	0	0	122,516
Marketable securities:				
Corporate notes and obligations	0	707,613	0	707,613
U.S. agency obligations	0	79,408	0	79,408
U.S. treasury securities	22,706	0	0	22,706
Government obligations	6,532	0	0	6,532
Mortgage backed securities	0	38,886	0	38,886
Collateralized mortgage obligations	0	105,039	0	105,039
Municipal securities	0	23,081	0	23,081
Foreign currency derivative contracts (2)	0	1,539	0	1,539
Total Assets	\$ 178,319	\$ 955,566	\$ 0	\$ 1,133,885
Liabilities				
Foreign currency derivative contracts (3)	\$ 0	\$ 2,863	\$ 0	\$ 2,863
Contingent considerations (related to acquisitions, see Note 4) (3)	0	0	17,138	17,138
Total Liabilities	\$ 0	\$ 2,863	\$ 17,138	\$ 20,001

- (1) Included in cash and cash equivalents in the accompanying Condensed Consolidated Balance Sheet as of January 31, 2011, in addition to \$275.2 million of cash.
- (2) Included in prepaid expenses and other current assets in the accompanying Condensed Consolidated Balance Sheet as of January 31, 2011.
- (3) Included in accrued expenses and other current liabilities in the accompanying Condensed Consolidated Balance Sheet as of January 31, 2011.

The following table presents the Company's only liability measured at fair value using significant unobservable inputs (Level 3) at January 31, 2011. This liability consists of the Company's contingent considerations related to acquisitions and the fair value was determined using a discounted cash flow model (in thousands):

Balance at February 1, 2010	\$ 0
Additions	17,138
Balance at January 31, 2011	\$ 17,138

Strategic Investments

The Company has one investment in a marketable equity security measured using its quoted price in its active market (Level 1) and certain interests in non-marketable equity securities that the Company considers strategic investments. The fair value of the Company's marketable security of \$6.0 million includes an unrealized loss of

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Notes to Condensed Consolidated Financial Statements (Continued)

\$0.4 million for the three months ended April 30, 2011. The total carrying value that approximates the fair value of the Company's strategic investments was \$31.6 million and \$27.1 million as of April 30, 2011 and January 31, 2011, respectively. Strategic investments are recorded in Other Assets, net on the condensed consolidated balance sheet.

Derivative Financial Instruments

The Company enters into foreign currency derivative contracts with financial institutions to reduce the risk that its cash flows and earnings will be adversely affected by foreign currency exchange rate fluctuations. The Company uses forward currency derivative contracts to minimize the Company's exposure of balances denominated in Euros, Swiss francs, Australian dollars, Singapore dollars, Japanese yen and British pounds. The Company's foreign currency derivative contracts which are not designated as hedging instruments are used to reduce the exchange rate risk associated primarily with intercompany receivables and payables. The Company's program is not designated for trading or speculative purposes. As of April 30, 2011 and January 31, 2011 the foreign currency derivative contracts that were not settled are recorded at fair value on the condensed consolidated balance sheet.

Foreign currency derivative contracts are marked-to-market at the end of each reporting period with gains and losses recognized as other income (expense) to offset the gains or losses resulting from the settlement or remeasurement of the underlying foreign currency denominated receivables and payables. While the contract or notional amount is often used to express the volume of foreign currency derivative contracts, the amounts potentially subject to credit risk are generally limited to the amounts, if any, by which the counterparties' obligations under the agreements exceed the obligations of the Company to the counterparties.

Details on outstanding foreign currency derivative contracts related primarily to intercompany receivables and payables are presented below (in thousands):

	April 30, 2011	January 31, 2011
Notional amount of foreign currency derivative contracts	\$ 258,487	\$ 202,491
Fair value of foreign currency derivative contracts	\$ (4,266)	\$ (1,324)

The Company's fair value of its outstanding derivative instruments are summarized below (in thousands):

	Balance Sheet Location	Fair Value of Derivative Instruments	
		As of April 30, 2011	As of January 31, 2011
Derivative Assets			
Derivatives not designated as hedging instruments:			
Foreign currency derivative contracts	Prepaid expenses and other current assets	\$ 407	\$ 1,539
Derivative Liabilities			
Derivatives not designated as hedging instruments:			
Foreign currency derivative contracts	Accrued expenses and other current liabilities	\$ 4,673	\$ 2,863

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Notes to Condensed Consolidated Financial Statements (Continued)

The effect of the derivative instruments not designated as hedging instruments on the Condensed Consolidated Statements of Operations for the three months ended April 30, 2011 and 2010, respectively are summarized below (in thousands):

Derivatives Not Designated as Hedging Instruments	Gains (Losses) Recognized in Income on Derivative Instruments Three months ended April 30,		
	Location	2011	2010
Foreign currency derivative contracts	Other expense	\$ (11,042)	\$ 2,082

Investment Income

Investment income consists of interest income, realized gains, and realized losses on the Company's cash, cash equivalents and marketable securities. The components of investment income are presented below (in thousands):

(In thousands)	Three months ended April 30,	
	2011	2010
Interest income	\$ 6,263	\$ 4,993
Realized gains	3,271	3,200
Realized losses	(1,479)	(318)
Total investment income	\$ 8,055	\$ 7,875

Comprehensive Income (loss)

Comprehensive income (loss) consists of the following, net of tax: net income, net foreign currency translation gains and losses, and net unrealized gains and losses on marketable securities. The following table sets forth the components of comprehensive income (in thousands):

	Three months ended April 30,	
	2011	2010
Consolidated net income	\$ 530	\$ 19,876
Less: net income attributable to noncontrolling interest	0	(2,131)
Translation and other adjustments	(7,077)	2,432
Unrealized gain (loss) on marketable securities, net	434	(932)
Comprehensive income (loss) attributable to salesforce.com	\$ (6,113)	\$ 19,245

Net Income Per Share

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Basic net income per share attributable to salesforce.com is computed by dividing net income attributable to salesforce.com by the weighted-average number of common shares outstanding for the fiscal period. Diluted net income per share attributable to salesforce.com is computed giving effect to all potential weighted average dilutive common stock, including options, restricted stock units, warrants and the convertible senior notes. The dilutive effect of outstanding awards is reflected in diluted earnings per share by application of the treasury stock method.

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Notes to Condensed Consolidated Financial Statements (Continued)

A reconciliation of the denominator used in the calculation of basic and diluted net income per share attributable to salesforce.com is as follows (in thousands):

	Three months ended April 30,	
	2011	2010
Numerator:		
Net income attributable to salesforce.com	\$ 530	\$ 17,745
Denominator:		
Weighted-average shares outstanding for basic earnings per share	133,454	128,032
Effect of dilutive securities:		
Convertible senior notes	2,409	0
Employee stock awards	4,521	4,219
Warrants	678	0
Adjusted weighted-average shares outstanding and assumed conversions for diluted earnings per share	141,062	132,251

As the weighted average market value per share of the Company's common stock for the quarter ended April 30, 2011 exceeds the strike price of the Notes and the Warrants, both instruments had a dilutive effect on the Company's earnings per share for the quarter ended April 30, 2011. Dilutive shares outstanding during the three month period ended April 30, 2010 do not include any effect resulting from the Notes as the Company's common stock did not exceed the strike price or from the warrants as their impact would have been anti-dilutive. The following were excluded from the computation of diluted shares outstanding as they would have had an anti-dilutive impact. The dilutive securities are excluded when, for example, their exercise prices, unrecognized compensation and tax benefits are greater than the average fair values of the Company's common stock (in thousands). These securities could be included in the future if the average market value of the Company's common stock increases and is greater than the exercise price.

	Three months ended April 30,	
	2011	2010
Stock awards	2,537	3,341
Warrants	0	6,736
Income Taxes		

The Company uses the liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on temporary differences between the financial statement and tax basis of assets and liabilities and net operating loss and credit carryforwards using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts more likely than not expected to be realized.

The total income tax benefit recognized in the accompanying condensed consolidated statements of operations related to stock-based awards was \$16.5 million and \$9.7 million for the three months ended April 30, 2011 and 2010 respectively.

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Notes to Condensed Consolidated Financial Statements (Continued)

Effective Tax Rate

The Company computes its provision for income taxes by applying the estimated annual effective tax rate to income from recurring operations and adjusts the provision for discrete tax items recorded in the period. The Company's effective tax rate for the three months ended April 30, 2011 was 32 percent, which was lower than the federal statutory tax rate of 35 percent. The lower tax rate was attributable to the benefit of federal and California research tax credits offset by state income taxes, a detrimental foreign tax rate differential and non-deductible acquisition expenses.

The Company's effective tax rate of 38 percent for the three months ended April 30, 2010 was higher than the federal statutory rate of 35 percent primarily due to state income taxes, a detrimental foreign tax rate differential and the unfavorable impact of a change in California tax law, which was partially offset by the benefit of California research tax credits.

Unrecognized Tax Benefits and Other Considerations

The Company records liabilities related to its uncertain tax positions. The Company's existing tax positions will continue to generate an increase in tax liabilities or unrecognized tax benefits. The Company does not believe that it is reasonably possible that there will be a significant increase or decrease in unrecognized tax benefits over the next twelve months.

Tax positions for the Company and its subsidiaries are subject to income tax audits by multiple tax jurisdictions throughout the world. The Company does not believe that it is reasonably possible that the estimates of unrecognized tax benefits will change significantly in the next twelve months. However, an adverse resolution of one or more uncertain tax positions in any period could have a material impact on the results of operations for that period.

Revenue Recognition

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

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

There is persuasive evidence of an arrangement;

The service has been or is being provided to the customer;

The collection of the fees is reasonably assured; and

The amount of fees to be paid by the customer is fixed or determinable.

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

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Notes to Condensed Consolidated Financial Statements (Continued)

Subscription and Support Revenues

Subscription and support revenues are recognized ratably over the contract terms beginning on the commencement date of each contract, which is the date the Company's service is made available to customers. Amounts that have been invoiced are recorded in accounts receivable and in deferred revenue or revenue, depending on whether the revenue recognition criteria have been met.

Professional Services and Other Revenues

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

Multiple-Deliverable Arrangements

The Company enters into arrangements with multiple deliverables that generally include subscription, premium support, and professional services.

Prior to February 1, 2011, the deliverables in multiple-deliverable arrangements were accounted for separately if the delivered items had standalone value and there was objective and reliable evidence of fair value for the undelivered items. If the deliverables in a multiple-deliverable arrangement could not be accounted for separately, the total arrangement fee was recognized ratably as a single unit of accounting over the contracted term of the subscription agreement. A significant portion of the Company's multiple-deliverable arrangements were accounted for as a single unit of accounting because the Company did not have objective and reliable evidence of fair value for certain of its deliverables. Additionally, in these situations, the Company deferred the direct costs of a related professional service arrangement and amortized those costs over the same period as the professional services revenue was recognized.

In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2009-13, *Revenue Recognition (Topic 605), Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force* (ASU 2009-13) which amended the previous multiple-deliverable arrangements accounting guidance. Pursuant to the new guidance, objective and reliable evidence of fair value of the deliverables to be delivered is no longer required in order to account for deliverables in a multiple-deliverable arrangement separately. Instead, arrangement consideration is allocated to deliverables based on their relative selling price. The new guidance also eliminates the use of the residual method.

In the first quarter of fiscal 2012, the Company adopted this new accounting guidance on a prospective basis. The Company applied the new accounting guidance to those multiple-deliverable arrangements entered into or materially modified on or after February 1, 2011 which is the beginning of the Company's fiscal year.

The adoption of this new accounting guidance did not have a material impact on the Company's financial condition, results of operations or cash flows. As of April 30, 2011, the deferred professional services revenue and deferred costs under the previous accounting guidance are \$58.7 million and \$27.5 million respectively which will continue to be recognized over the related remaining subscription period.

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Under the new accounting guidance, in order to treat deliverables in a multiple-deliverable arrangement as separate units of accounting, the deliverables must have standalone value upon delivery. If the deliverables have standalone value upon delivery, the Company accounts for each deliverable separately. Subscription services have standalone value as such services are often sold separately. In determining whether professional services have standalone value, the Company considers the following factors for each professional services agreement: availability of the services from other vendors, the nature of the professional services, the timing of when the professional services contract was signed in comparison to the subscription service start date, and the contractual dependence of the subscription service on the customer's satisfaction with the professional services work. To date, the Company has concluded that all of the professional services included in multiple-deliverable arrangements executed have standalone value.

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

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

The Company determined BESP by considering its overall pricing objectives and market conditions. Significant pricing practices taken into consideration include the Company's discounting practices, the size and volume of the Company's transactions, the geographic area where services are sold, price lists, its go to market strategy, historic contractually stated prices and prior relationships and future subscription service sales with certain classes of customers. The determination of BESP is made through consultation with and approval by the Company's management, taking into consideration the go-to market strategy. As the Company's go-to-market strategies evolve, the Company may modify its pricing practices in the future, which could result in changes in selling prices, including both VSOE and BESP.

Deferred Revenue

Deferred revenue primarily consists of billings or payments received in advance of revenue recognition from subscription service described above and is recognized as the revenue recognition criteria are met. The Company generally invoices customers in annual or quarterly installments.

Accordingly, the deferred revenue balance does not represent the total contract value of annual or multi-year, non-cancelable subscription agreements.

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Billings against professional services arrangements entered into prior to February 1, 2011 will generally be added to deferred revenue and recognized over the remaining related subscription contract term.

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

Deferred Commissions

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

The commissions are deferred and amortized over the non-cancelable terms of the related customer contracts, which are typically 12 to 24 months. The commission payments are paid in full the month after the customer's service commences. The deferred commission amounts are recoverable through the future revenue streams under the non-cancelable customer contracts. The Company believes this is the preferable method of accounting as the commission charges are so closely related to the revenue from the non-cancelable customer contracts that they should be recorded as an asset and charged to expense over the same period that the subscription revenue is recognized. Amortization of deferred commissions is included in marketing and sales expense in the accompanying condensed consolidated statements of operations.

Business Combinations

The Company recognizes separately from goodwill the fair value of assets acquired and liabilities assumed. Goodwill as of the acquisition date is measured as the excess of consideration transferred and the net of the acquisition date fair values of the assets acquired and the liabilities assumed. While the Company uses its best estimates and assumptions as a part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the acquisition date, the Company's estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, the Company may record adjustments to the fair value of assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period or final determination of the fair value of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the Company's condensed consolidated statements of operations.

In addition, uncertain tax positions and tax related valuation allowances assumed in connection with a business combination are initially estimated as of the acquisition date. The Company reevaluates these items quarterly and records any adjustments to the Company's preliminary estimates to goodwill provided that the Company is within the measurement period and the Company continues to collect information in order to determine their estimated fair values as of the date of acquisition. Subsequent to the measurement period or the Company's final determination of the tax allowance's or contingency's estimated value, changes to these uncertain tax positions and tax related valuation allowances will affect the Company's provision for income taxes in the Company's condensed consolidated statement of operations.

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Notes to Condensed Consolidated Financial Statements (Continued)***Accounting for Stock-Based Compensation***

The Company recognizes stock-based expenses on a straight-line basis over the requisite service period of the awards, which is the vesting term of four years. Stock-based expenses are recognized net of estimated forfeiture activity.

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

	Three months ended April 30,	
	2011	2010
Volatility	50%	50%
Estimated life	3.7 years	3.8 years
Risk-free interest rate	1.56-1.77%	2.00-2.11%
Dividend yield	0	0
Weighted-average fair value per share of grants	\$ 52.72	\$ 28.76

The estimated life was based on an actual analysis of expected life. The risk free interest rate is based on the rate for a four-year U.S. government security at the time of the option grant.

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

During the three months ended April 30, 2011 and 2010, the Company capitalized \$0.7 million and \$0.7 million, respectively, of stock-based expenses related to capitalized internal-use software development and deferred professional services costs.

During the three months ended April 30, 2011, the Company recognized stock-based expense of \$47.6 million. As of April 30, 2011, the aggregate stock compensation remaining to be amortized to costs and expenses was \$542.1 million. The Company expects this stock compensation balance to be amortized as follows: \$150.8 million during the remaining nine months of fiscal 2012; \$166.5 million during fiscal 2013; \$138.3 million during fiscal 2014; \$85.4 million during fiscal 2015 and \$1.1 million during fiscal 2016. The expected amortization reflects only outstanding stock awards as of April 30, 2011 and assumes no forfeiture activity. The Company expects to continue to issue stock-based awards to its employees in future periods.

Goodwill, Intangible Assets and Impairment Assessments

Goodwill represents the excess of the purchase price of an acquired business over the fair value of the underlying net tangible and intangible assets. Goodwill is tested for impairment at least annually (more frequently if certain indicators are present). In the event that the Company determines that the carrying value of goodwill is less than fair value, the Company will incur an impairment charge for the amount of the difference during the quarter in which the determination is made.

Intangible assets are amortized over their useful lives. Each period the Company evaluates the estimated remaining useful life of its intangible assets and whether events or changes in circumstances warrant a revision to the remaining period of amortization. The carrying amounts of these assets are periodically reviewed for

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Notes to Condensed Consolidated Financial Statements (Continued)

impairment whenever events or changes in circumstances indicate that the carrying value of these assets may not be recoverable. Recoverability of these assets is measured by comparison of the carrying amount of each asset to the future undiscounted cash flows the asset is expected to generate. In the event that the Company determines certain assets are not fully recoverable, the Company will incur an impairment charge for those assets or portion thereof during the quarter in which the determination is made.

Warranties and Indemnification

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

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

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

Subsequent Events

The Company evaluated subsequent events through the date this Quarterly Report on Form 10-Q was filed with the SEC.

On May 2, 2011 the Company acquired for cash and stock the outstanding stock of Radian6 Technologies Inc. (Radian6), a cloud application vendor based in Canada that provides customers with social media monitoring, measurement and engagement solutions. The Company acquired Radian6 for the assembled workforce, expected synergies and expanded market opportunities when integrating Radian6's social solution technology with the Company's current offerings. Beginning with the fiscal quarter ended July 31, 2011, the Company will include the financial results of Radian6 in its condensed consolidated financial statements from the date of acquisition. The total purchase price for Radian6 was approximately \$344.5 million net of cash acquired, of which \$285.1 million was paid in cash and the remainder in 436,167 shares of salesforce.com common stock. As part of the share purchase agreement, the Company also assumed Radian6's existing stock option plan which, after giving effect to the acquisition, consisted of options to purchase 239,519 shares of the Company's common stock.

New Accounting Pronouncement

In December 2010, the FASB issued Accounting Standards Update No. 2010-29, *Disclosure of Supplementary Pro Forma Information for Business Combinations (Topic 805) Business Combinations* (ASU 2010-29), to improve consistency in how the pro forma disclosures are calculated. Additionally, ASU

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Notes to Condensed Consolidated Financial Statements (Continued)

2010-29 enhances the disclosure requirements and requires description of the nature and amount of any material, nonrecurring pro forma adjustments directly attributable to a business combination. ASU 2010-29 is effective for the Company in fiscal 2013 and should be applied prospectively to business combinations for which the acquisition date is after the effective date. Early adoption is permitted. The Company is currently evaluating the impact of the pending adoption of ASU 2010-29 on the consolidated financial statements.

Reclassification

A reclassification to the quarter ending April 30, 2010, condensed consolidated statement of cash flows was made. This reclassification was related to the purchase of subsidiary stock.

2. Balance Sheet Accounts**Marketable Securities**

At April 30, 2011, marketable securities consisted of the following (in thousands):

Investments classified as Marketable Securities	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate notes and obligations	\$ 595,475	\$ 7,464	\$ (243)	\$ 602,696
U.S. treasury securities	26,756	88	(6)	26,838
Mortgage backed securities	36,027	731	(74)	36,684
Government obligations	6,384	153	0	6,537
Municipal securities	25,126	95	(61)	25,160
Collateralized mortgage obligations	91,623	1,266	(287)	92,602
U.S. agency obligations	66,992	170	(6)	67,156
Total marketable securities	\$ 848,383	\$ 9,967	\$ (677)	\$ 857,673

At January 31, 2011, marketable securities consisted of the following (in thousands):

Investments classified as Marketable Securities	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate notes and obligations	\$ 701,047	\$ 7,356	\$ (790)	\$ 707,613
U.S. treasury securities	22,631	85	(10)	22,706
Mortgage backed securities	38,348	656	(118)	38,886
Government obligations	6,414	118	0	6,532
Municipal securities	23,121	79	(119)	23,081
Collateralized mortgage obligations	104,285	1,098	(344)	105,039
U.S. agency obligations	79,242	190	(24)	79,408
Total marketable securities	\$ 975,088	\$ 9,582	\$ (1,405)	\$ 983,265

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

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	April 30, 2011	January 31, 2011
Recorded as follows (in thousands):		
Short-term (due in one year or less)	\$ 99,224	\$ 72,678
Long-term (due between one and 3 years)	758,449	910,587
	\$ 857,673	\$ 983,265

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Notes to Condensed Consolidated Financial Statements (Continued)

As of April 30, 2011, the following marketable securities were in an unrealized loss position (in thousands):

	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate notes and obligations	\$ 63,272	\$ (242)	\$ 303	\$ (1)	\$ 63,575	\$ (243)
U.S. treasury securities	1,837	(6)	0	0	1,837	(6)
Mortgage backed securities	5,986	(54)	3,729	(20)	9,715	(74)
Municipal securities	6,150	(61)	0	0	6,150	(61)
Collateralized mortgage obligations	25,149	(286)	163	(1)	25,312	(287)
U.S. agency obligations	5,546	(6)	0	0	5,546	(6)
	\$ 107,940	\$ (655)	\$ 4,195	\$ (22)	\$ 112,135	\$ (677)

The unrealized loss for each of these fixed rate marketable securities ranged from less than \$1,000 to \$139,000. The Company does not believe any of the unrealized losses represent an other-than-temporary impairment based on its evaluation of available evidence as of April 30, 2011. The Company expects to receive the full principal and interest on all of these marketable securities.

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consisted of the following (in thousands):

	April 30, 2011	January 31, 2011
Deferred professional services costs	\$ 17,645	\$ 17,908
Prepaid expenses and other current assets	46,241	37,813
	\$ 63,886	\$ 55,721

Property and Equipment

Property and equipment consisted of the following (in thousands):

	April 30, 2011	January 31, 2011
Land	\$ 248,263	