

8X8 INC /DE/
Form 10-Q
July 29, 2016

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

FORM 10-Q

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

For the quarterly period ended June 30, 2016

OR

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 000-21783

[8X8, INC.](#)

(Exact name of Registrant as Specified in its Charter)

Delaware

(State or Other Jurisdiction of Incorporation or Organization)

77-0142404

(I.R.S. Employer Identification Number)

2125 O'Nel Drive
San Jose, CA 95131

(Address of Principal Executive Offices)

(408) 727-1885

(Registrant's Telephone Number, including Area Code)

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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 reports), and (2) has been subject to such filing requirements for the past 90 days. x 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 (§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 "

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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer " Non-accelerated filer " Smaller reporting company
x (Do not check if a 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 x

The number of shares of the Registrant's Common Stock outstanding as of July 25, 2016 was 89,680,865.

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Part I -- FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

8X8, Inc.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, unaudited)

	June 30, 2016	March 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 27,466	\$ 33,576
Short-term investments	139,607	129,274
Accounts receivable, net	11,538	11,070
Inventory	463	520
Deferred cost of goods sold	717	634
Deferred income taxes	-	5,382
Other current assets	5,096	5,444
Total current assets	184,887	185,900
Property and equipment, net	13,015	12,375
Intangible assets, net	19,531	21,464
Goodwill	45,931	47,420
Non-current deferred income taxes	48,532	43,189
Other assets	3,751	3,104
Total assets	\$ 315,647	\$ 313,452
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 12,649	\$ 10,954
Accrued compensation	9,631	10,063
Accrued warranty	340	326
Accrued taxes	5,390	5,200
Accrued outside commissions	2,070	2,186
Deferred revenue	2,120	1,925
Other accrued liabilities	3,226	4,080
Total current liabilities	35,426	34,734
Non-current liabilities	3,107	3,258
Non-current deferred revenue	134	154
Total liabilities	38,667	38,146
Commitments and contingencies (Note 6)		
Stockholders' equity:		
Common stock	89	89
Additional paid-in capital	394,100	389,260
Accumulated other comprehensive loss	(6,822)	(4,184)
Accumulated deficit	(110,387)	(109,859)
Total stockholders' equity	276,980	275,306
Total liabilities and stockholders' equity	\$ 315,647	\$ 313,452

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

8X8, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share amounts; unaudited)

	Three Months Ended	
	June 30,	
	2016	2015
Service revenue	\$ 55,296	\$ 44,168
Product revenue	4,745	3,724
Total revenue	60,041	47,892
Operating expenses:		
Cost of service revenue	10,235	8,459
Cost of product revenue	5,505	4,382
Research and development	6,710	5,080
Sales and marketing	31,691	23,824
General and administrative	6,801	6,068
Total operating expenses	60,942	47,813
Income (loss) from operations	(901)	79
Other income, net	410	234
Income (loss) before provision for income taxes	(491)	313
Provision for income taxes	37	785
Net loss	\$ (528)	\$ (472)
Net loss per share:		
Basic	\$ (0.01)	\$ (0.01)
Diluted	\$ (0.01)	\$ (0.01)
Weighted average number of shares:		
Basic	89,434	88,233
Diluted	89,434	88,233

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

8X8, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands, unaudited)

	Three Months Ended	
	June 30,	
	2016	2015
Net loss	\$ (528)	\$ (472)
Other comprehensive income (loss), net of tax		
Unrealized gain (loss) on investments in securities	146	(48)
Foreign currency translation adjustment	(2,784)	1,478
Comprehensive income (loss)	\$ (3,166)	\$ 958

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

8X8, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands, unaudited)

	Three Months Ended June 30,	
	2016	2015
Cash flows from operating activities:		
Net loss	\$ (528)	\$ (472)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation	1,471	993
Amortization of intangible assets	960	546
Amortization of capitalized software	146	456
Net accretion of discount and amortization of premium on marketable securities	100	236
Stock-based compensation expense	5,051	3,022
Deferred income tax (benefit) provision	(44)	476
Other	190	74
Changes in assets and liabilities:		
Accounts receivable, net	(1,043)	(612)
Inventory	53	88
Other current and noncurrent assets	(508)	(470)
Deferred cost of goods sold	(120)	(53)
Accounts payable	1,137	933
Accrued compensation	(354)	725
Accrued warranty	14	3
Accrued taxes	240	492
Deferred revenue	211	(704)
Accrued outside commissions	(116)	199
Other current and noncurrent liabilities	(324)	(1,272)
Net cash provided by operating activities	6,536	4,660
Cash flows from investing activities:		
Purchases of property and equipment	(1,604)	(1,073)
Cost of capitalized software	(707)	(471)
Purchase of businesses, net of cash acquired	-	(23,434)
Proceeds from maturity of investments	17,025	7,820
Sales of investments - available for sale	15,324	22,620
Purchase of investments - available for sale	(42,625)	(34,409)
Net cash used in investing activities	(12,587)	(28,947)
Cash flows from financing activities:		
Capital lease payments	(182)	(54)
Payment of contingent consideration and escrow	(200)	-
Repurchase of common stock	(629)	(25)
Proceeds from issuance of common stock under employee stock plans	1,039	336
Net cash provided by financing activities	28	257
Effect of exchange rate changes on cash	(87)	218
Net decrease in cash and cash equivalents	(6,110)	(23,812)
Cash and cash equivalents, beginning of the period	33,576	53,110
Cash and cash equivalents, end of the period	\$ 27,466	\$ 29,298
Supplemental cash flow information		
Income taxes paid	\$ 87	\$ 52
Interest paid	7	6

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

8X8, Inc.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

DESCRIPTION OF BUSINESS

8x8, Inc. (8x8 or the Company) is a provider of cloud-based, enterprise-class software solutions that transform the way businesses communicate and collaborate globally. The Company's integrated, "pure-cloud" offering combines global voice, conferencing, messaging and video with integrated workflows and big data analytics on a single platform to enable increased team productivity, better customer engagement and real-time insights into business performance.

BASIS OF PRESENTATION

The Company's fiscal year ends on March 31 of each calendar year. Each reference to a fiscal year in these notes to the consolidated financial statements refers to the fiscal year ended March 31 of the calendar year indicated (for example, fiscal 2017 refers to the fiscal year ended March 31, 2017).

The accompanying interim condensed consolidated financial statements are unaudited and have been prepared on substantially the same basis as our annual consolidated financial statements for the fiscal year ended March 31, 2016. In the opinion of the Company's management, these interim condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair statement of our financial position, results of operations and cash flows for the periods presented. The preparation of financial statements in conformity with generally accepted accounting principles 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 revenue and expenses during the reporting periods. Actual results could differ from these estimates.

The March 31, 2016 year-end condensed consolidated balance sheet data in this document were derived from audited consolidated financial statements and does not include all of the disclosures required by U.S. generally accepted accounting principles. These condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements as of and for the fiscal year ended March 31, 2016 and notes thereto included in the Company's fiscal 2016 Annual Report on Form 10-K.

The results of operations and cash flows for the interim periods included in these condensed consolidated financial statements are not necessarily indicative of the results to be expected for any future period or the entire fiscal year.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of 8x8 and its subsidiaries. All material intercompany accounts and transactions have been eliminated.

SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies used in preparation of these condensed consolidated financial statements are disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2016 filed with the SEC on May 31, 2016, and there have been no changes to the Company's significant accounting policies during the three months ended June 30, 2016, except as described in the "Recently Adopted Accounting Pronouncements" section below.

RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

In April 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-5, *"Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement."* This update provides guidance in evaluating whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the software license element of the arrangement should be accounted for as an acquisition of a software license. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The guidance does not change generally accepted accounting principles for a customer's accounting for service contracts. This update is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2015. Therefore, the Company has prospectively adopted this new standard on April 1, 2016. The adoption of this standard did not have a material impact on our consolidated financial statements.

In November 2015, the FASB issued ASU 2015-17, *Income Taxes - Balance Sheet Classification of Deferred Taxes (Topic 740)*. This ASU requires all deferred tax liabilities and assets to be presented in the balance sheet as noncurrent. As permitted, the Company early adopted this standard prospectively during the quarter ended June 30, 2016. The adoption of this standard resulted in reclassifying current deferred income tax assets to noncurrent deferred income tax assets and current deferred income tax liabilities to noncurrent deferred income tax liabilities. No prior periods were retrospectively adjusted.

RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard will become effective for the Company on April 1, 2018. The standard permits the use of either the retrospective or cumulative effect transition method. The Company has not yet selected a transition method.

In April 2016, the FASB issued ASU No. 2016-10, *Revenue from Contracts with Customers (Topic 606) - Identifying Performance Obligations and Licensing*. The ASU amends the guidance in ASU 2014-09 related to identifying performance obligations and accounting for licenses of intellectual property.

In May 2016, the FASB issued ASU No. 2016-12, *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*. The amendment provides clarifying guidance in certain narrow areas and adds some practical expedients.

The Company is currently assessing the impact of this pronouncement and its amendments to its consolidated financial statements.

2. FAIR VALUE MEASUREMENTS

Cash, cash equivalents, and available-for-sale investments, and contingent consideration were (in thousands):

	Amortized Costs	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value	Cash and Cash Equivalents	Short-Term Investments
As of June 30, 2016						
Cash	\$ 22,440	\$ -	\$ -	\$ 22,440	\$ 22,440	\$ -
Level 1:						
Money market funds	5,026	-	-	5,026	5,026	-
Mutual funds	2,000	-	(175)	1,825	-	1,825
Subtotal	29,466	-	(175)	29,291	27,466	1,825
Level 2:						
Commercial paper	15,660	8	-	15,668	-	15,668
Corporate debt	88,620	143	(10)	88,753	-	88,753
Municipal securities	1,001	-	(1)	1,000	-	1,000
Asset backed securities	27,349	32	(1)	27,380	-	27,380
Mortgage backed securities	1,989	-	(14)	1,975	-	1,975
Agency bond	2,000	5	-	2,005	-	2,005
International government securities	1,000	1	-	1,001	-	1,001
Subtotal	137,619	189	(26)	137,782	-	137,782
Total assets	\$ 167,085	\$ 189	\$ (201)	\$ 167,073	\$ 27,466	\$ 139,607
Level 3:						
Contingent consideration	\$ -	\$ -	\$ -	\$ 216	\$ -	\$ -
Total liabilities	\$ -	\$ -	\$ -	\$ 216	\$ -	\$ -
			8			
As of March 31, 2016						
Cash	\$ 18,596	\$ -	\$ -	\$ 18,596	\$ 18,596	\$ -
Level 1:						
Money market funds	14,980	-	-	14,980	14,980	-
Mutual funds	2,000	-	(187)	1,813	-	1,813
Subtotal	35,576	-	(187)	35,389	33,576	1,813
Level 2:						
Commercial paper	6,794	2	-	6,796	-	6,796
Corporate debt	85,164	78	(28)	85,214	-	85,214
Municipal securities	1,007	-	(1)	1,006	-	1,006
Asset backed securities	24,614	7	(11)	24,610	-	24,610
Mortgage backed securities	2,045	-	(17)	2,028	-	2,028
Agency bond	6,805	1	-	6,806	-	6,806
International government securities	1,000	1	-	1,001	-	1,001
Subtotal	127,429	89	(57)	127,461	-	127,461
Total assets	\$ 163,005	\$ 89	\$ (244)	\$ 162,850	\$ 33,576	\$ 129,274
Level 3:						
Contingent consideration	\$ -	\$ -	\$ -	\$ 341	\$ -	\$ -
Total liabilities	\$ -	\$ -	\$ -	\$ 341	\$ -	\$ -

Contractual maturities of investments as of June 30, 2016 are set forth below (in thousands):

	Estimated Fair Value
Due within one year	\$ 79,772
Due after one year	59,835
Total	\$ 139,607

Contingent Consideration and Escrow Liability

The Company's contingent consideration liability and escrow liability, included in other accrued liabilities and noncurrent liabilities on the consolidated balance sheets, was associated with the Quality Software Corporation (QSC) acquisition made in the first quarter of fiscal 2016. Amounts held in escrow were measure at fair value using present value computations. The contingent consideration was measured at fair value using a probability weighted average of the potential payment outcomes that would occur should certain contract milestones be reached. There is no market data available to use in valuing the contingent consideration; therefore, the Company developed its own assumptions related to the achievement of the milestones to evaluate the fair value of the liability. As such, the contingent consideration is classified within Level 3 as described below.

The items are classified as Level 3 within the valuation hierarchy, consisting of contingent consideration and escrow liability related to the QSC acquisition, were valued based on an estimate of the probability of success of the milestones being achieved and present value computations, respectively. The table below presents a roll-forward of the contingent consideration and escrow liability valued using a Level 3 input (in thousands):

	Three Months Ended June 30, 2016	Year Ended March 31, 2016
Balance at beginning of period	\$ 341	\$ -
Purchase price contingent consideration	-	541
Contingent consideration payments	(125)	(200)
Balance at end of period	\$ 216	\$ 341

3. INVENTORIES

	June 30, 2016	March 31, 2016
Inventory (in thousands)		
Work-in-process	\$ 3	\$ 76
Finished goods	460	444
Total	\$ 463	\$ 520

4. INTANGIBLE ASSETS AND GOODWILL

The carrying value of intangible assets consisted of the following (in thousands):

	June 30, 2016			March 31, 2016		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Technology	\$ 18,033	\$ (5,215)	\$ 12,818	\$ 18,640	\$ (4,622)	\$ 14,018
Customer relationships	9,716	(5,215)	4,501	9,993	(4,847)	5,146
Trade names/domains	2,117	-	2,117	2,205	-	2,205
In-process research and development	95	-	95	95	-	95
Total acquired identifiable intangible assets	\$ 29,961	\$ (10,430)	\$ 19,531	\$ 30,933	\$ (9,469)	\$ 21,464

At June 30, 2016, annual amortization of intangible assets, based upon our existing intangible assets and current useful lives, is estimated to be the following (in thousands):

	Amount
Remaining 2017	\$ 2,758
2018	3,411
2019	3,162
2020	3,162
2021	2,796
Thereafter	2,030
Total	\$ 17,319

The following table provides a summary of the changes in the carrying amounts of goodwill by reporting segment (in thousands):

	Americas	Europe	Total
Balance as of March 31, 2016	\$ 25,729	\$ 21,691	\$ 47,420
Foreign currency translation	-	(1,489)	(1,489)
Balance as of June 30, 2016	\$ 25,729	\$ 20,202	\$ 45,931

5. RESEARCH, DEVELOPMENT AND SOFTWARE COSTS

In the first three months of fiscal 2017 and 2016, the Company expensed all research and development costs in accordance with ASC 985-20, *Costs of Software to be Sold, Leased or Marketed* (ASC 985-20).

The Company accounts for computer software developed or obtained for internal use in accordance with ASC 350-40, *Internal Use Software* (ASC 350-40). Capitalized costs are classified as either long-term assets or property and equipment on the consolidated balance sheets.

Other Long-Term Assets

In the first three months of fiscal 2017, the Company capitalized \$0.7 million as other long-term assets. In the first three months of fiscal 2016, the Company capitalized \$0.5 million as other long-term assets. At June 30, 2016 and March 31, 2016, total completed capitalized software development costs included in other long-term assets was approximately \$1.7 million and \$0, respectively. At June 30, 2016 and March 31, 2016, accumulated amortization costs related to capitalized software in other long term assets was approximately \$0.1 million and \$0, respectively.

Property and Equipment

In the first three months of fiscal 2017, the Company capitalized \$0.3 million as property and equipment. The Company did not capitalize any costs in property and equipment in accordance with ASC 350-40 in the first three months of fiscal 2016. At June 30, 2016 and March 31, 2016, total completed capitalized software costs included in property and equipment was approximately \$1.2 million. At June 30, 2016 and March 31, 2016, accumulated amortization costs related to capitalized software in property and equipment was approximately \$0.3 million and \$0.2 million, respectively.

6. COMMITMENTS AND CONTINGENCIES

Leases

The Company leases its headquarters facility in San Jose, California under an operating lease agreement that expires in October 2019. The lease is an industrial net lease with monthly base rent of \$130,821 for the first 15 months with a 3% increase each year thereafter, and requires us to pay property taxes, utilities and normal maintenance costs. The Company also leases facilities for office space under non-cancelable operating leases for its various domestic and international locations.

The Company has entered into a series of noncancelable capital lease agreements for office equipment bearing interest at various rates. Assets under capital lease at June 30, 2016 totaled \$1.6 million with accumulated amortization of \$0.6 million.

Guarantees

Indemnifications

In the normal course of business, the Company may agree to indemnify other parties, including customers, lessors and parties to other transactions with the Company, with respect to certain matters such as breaches of representations or covenants or intellectual property infringement or other claims made by third parties. These agreements may limit the time within which an indemnification claim can be made and the amount of the claim. In addition, the Company has entered into indemnification agreements with its officers and directors.

It is not possible to determine the maximum potential amount of the Company's exposure under these indemnification agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement. Historically, payments made by the Company under these agreements have not had a material impact on the Company's operating results, financial position or cash flows. Under some of these agreements, however, the Company's potential indemnification liability might not have a contractual limit.

Product Warranties

The Company accrues for the estimated costs that may be incurred under its product warranties upon revenue recognition. Changes in the Company's product warranty liability, which is included in cost of product revenues in the consolidated statements of income (loss), were as follows (in thousands):

	Three Months Ended June 30,	
	2016	2015
Balance at beginning of period	\$ 326	\$ 339
Accruals for warranties	114	98
Settlements	(87)	(83)
Adjustments	(13)	(12)
Balance at end of period	\$ 340	\$ 342

Minimum Third Party Customer Support Commitments

In the third quarter of 2010, the Company amended its contract with one of its third party customer support vendors containing a minimum monthly commitment of approximately \$0.4 million effective April 1, 2010. The agreement requires a 150-day notice to terminate. At June 30, 2016, the total remaining obligation upon a termination of the contract was \$2.2 million.

Minimum Third Party Network Service Provider Commitments

The Company has entered into contracts with multiple vendors for third party network service which expire on various dates in fiscal 2017 through 2020. At June 30, 2016, future minimum annual payments under these third party network service contracts were as follows (in thousands):

<u>Year ending March 31:</u>	
Remaining 2017	\$ 1,961
2018	981
2019	32
2020	8
Total minimum payments	\$ 2,982

Legal Proceedings

The Company, from time to time, is involved in various legal claims or litigation, including patent infringement claims that can arise in the normal course of the Company's operations. Pending or future litigation could be costly, could cause the diversion of management's attention and could upon resolution, have a material adverse effect on the Company's business, results of operations, financial condition and cash flows.

On February 22, 2011, the Company was named a defendant in Bear Creek Technologies, Inc. v. 8x8, Inc. et al., along with 20 other defendants. On August 17, 2011, the suit was dismissed without prejudice as to the Company under Rule 21 of the Federal Rules of Civil Procedure. On August 17, 2011, Bear Creek Technologies, Inc. refiled its suit against the Company in the United States District Court for the District of Delaware. Further, on November 28, 2012, the U.S. Patent & Trademark Office initiated a Reexamination proceeding with a Reexamination Declaration explaining that there is a substantial new question of patentability, based on four separate grounds and affecting each claim of the patent which is the basis for the complaint filed against us. On March 26, 2013, the USPTO issued a first Office Action in the Reexamination, with all claims of the '722 patent being rejected on each of the four separate grounds raised in the Request for Reexamination. On July 10, 2013, the Company filed an informational pleading in support of and joining a motion to stay the proceeding in the District Court; the District Court granted the motion on July 17, 2013, based on the possibility that at least one of the USPTO rejections will be upheld and considering the USPTO's conclusion that Bear Creek's patent suffers from a defective claim for priority. On March 24, 2014, the USPTO issued another Office Action in which the rejections of the claims were maintained. On August 15, 2014, the USPTO issued a Right of Appeal Notice, as the USPTO maintained all rejections of the patent claims.

On September 15, 2014, Bear Creek Technologies, Inc. filed a Notice of Appeal of this decision with the Patent Trial and Appeal Board. The case is currently on appeal. The Company believes that it has meritorious defenses to these claims and is presenting a vigorous defense, but the Company cannot estimate potential liability in this case at this early stage of litigation.

On April 16, 2015, the Company was named as a defendant in Slocumb Law Firm v. 8x8, Inc. The Slocumb Law Firm has alleged that it purchased certain business services from the Company that did not perform as advertised or expected, and has asserted causes of actions for fraud, breach of contract, violations of the Alabama Deceptive Trade Practices Act and negligence. On May 7, 2015, the Company filed a motion with the U.S. District Court for the Middle District of Alabama, seeking an order compelling the Slocumb Law Firm to arbitrate its claims against the Company in Santa Clara County, California pursuant to a clause mandating arbitration of disputes set forth in the terms and conditions to which Slocumb Law Firm agreed in connection with its purchase of business services from the Company. No briefing schedule or hearing date for the motion has been set as of this time. Discovery has not yet commenced in the case. The Company intends to vigorously defend against Slocumb Law Firm's claims.

State and Municipal Taxes

From time to time, the Company has received inquiries from a number of state and municipal taxing agencies with

respect to the remittance of sales, use, telecommunications, excise, and income taxes. Several jurisdictions currently are conducting tax audits of the Company's records. The Company collects or has accrued for taxes that it believes are required to be remitted. The amounts that have been remitted have historically been within the accruals established by the Company.

7. STOCK-BASED COMPENSATION

The following table summarizes stock-based compensation expense (in thousands):

	Three Months Ended	
	June 30,	
	2016	2015
Cost of service revenue	\$ 360	\$ 219
Cost of product revenue	-	-
Research and development	887	531
Sales and marketing	1,915	1,197
General and administrative	1,889	1,075
Total stock-based compensation expense related to employee stock options and employee stock purchases, pre-tax	5,051	3,022
Tax benefit	-	-
Stock-based compensation expense related to employee stock options and employee stock purchases, net of tax	\$ 5,051	\$ 3,022

Stock Options, Stock Purchase Right and Restricted Stock Unit Activity

Stock Option activity under all the Company's stock option plans for the three months ended June 30, 2016, is summarized as follows:

Number of	Weighted Average
------------------	-------------------------