

SEACHANGE INTERNATIONAL INC

Form 10-K

April 07, 2015

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended January 31, 2015

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

Commission File Number: 0-21393

SEACHANGE INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Delaware	04-3197974
(State or other jurisdiction	(IRS Employer
of incorporation or organization)	Identification No.)
50 Nagog Park, Acton, MA 01720	

(Address of principal executive offices, including zip code)

(978)-897-0100

(Registrant's telephone number, including area code)

Securities Registered Pursuant To Section 12(b) Of The Act:

Common Stock, \$.01 par value

Securities Registered Pursuant To Section 12(g) Of The Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or in any amendment to this Form 10-K.

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 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 July 31, 2014, the aggregate market value of the voting stock held by non-affiliates of the registrant, based upon the closing price for the registrant's Common Stock on the NASDAQ Global Select Market on such date was \$232,231,128. The number of shares of the registrant's Common Stock outstanding as of the close of business on April 2, 2015 was 33,299,577.

DOCUMENTS INCORPORATED BY REFERENCE:

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Portions of the definitive Proxy Statement filed no later than 120 days after the Company's fiscal year end pursuant to Regulation 14A are incorporated by reference into Part III of this Annual Report on Form 10-K.

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CAUTIONARY STATEMENT FOR PURPOSES OF THE SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

The statements contained in this Annual Report on Form 10-K (Form 10-K) of SeaChange International, Inc. (SeaChange, the Company, us, or we), including, but not limited to the statements contained in Item 1., *Business*, and Item 7., *Management's Discussion and Analysis of the Financial Condition and Results of Operations*, along with statements contained in other reports that we have filed with the Securities and Exchange Commission (the SEC), external documents and oral presentations, which are not historical facts, are considered to be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements which may be expressed in a variety of ways, including the use of forward looking terminology such as believe, expect, seek, intend, may, will, should, potential, continue, estimate, plan, or anticipate, or the negatives thereof, other variations thereon or compatible terminology, relate to, among other things, our transition to being a company that primarily provides software solutions, the effect of certain legal claims against us, projected changes in our revenues, earnings and expenses, exchange rate sensitivity, interest rate sensitivity, liquidity, product introductions, industry changes, general market conditions, our continued limited number of customers, geographic location of sales and a reduction in workforce and the impact thereof. We do not undertake any obligation to publicly update any forward-looking statements.

These forward-looking statements, and any forward looking statements contained in other public disclosures of the Company which make reference to the cautionary factors contained in this Form 10-K, are based on assumptions that involve risks and uncertainties and are subject to change based on the considerations described below. We discuss many of these risks and uncertainties in greater detail in Item 1A., *Risk Factors*, of this Form 10-K. These and other risks and uncertainties may cause our actual results, performance or achievements to differ materially from anticipated future results, performance or achievements expressed or implied by such forward-looking statements.

The following discussion should be read in conjunction with Part II, Item 7., *Management Discussion and Analysis of Financial Condition and Results of Operations*, and our financial statements and footnotes contained in this Form 10-K.

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PART I

Item 1. BUSINESS

General

SeaChange International, Inc., a Delaware corporation founded on July 9, 1993, is an industry leader in the delivery of multiscreen video. Our products and services facilitate the aggregation, licensing, management and distribution of video (primarily movies and television programming) and television advertising content to cable television system operators, telecommunications and media companies. We sell our software products and services worldwide, primarily to television service providers including: cable television system operators, such as Liberty Global, plc. (LGI), Comcast Corporation (Comcast), Cox Communications, Inc. (Cox) and Rogers Communications, Inc.; telecommunications companies, such as Verizon Communications, Inc., AT&T, Inc. and Eircom; and media companies such as BBC Worldwide.

Our products and services are designed to enable our customers to reduce capital and operating expenses, reduce subscriber turnover, and increase average revenue per subscriber by establishing new, revenue-generating subscription television services and advertising. Using our products and services, we believe our customers can increase their revenues by offering services such as video-on-demand (VOD) television programming on a variety of consumer devices, including mobile telephones (smart phones), personal computers (PCs), tablets and over-the-top (OTT) streaming players. Our systems enable television service providers to offer other interactive television services that allow subscribers to receive personalized services and interact with their video devices, thereby enhancing their viewing experience. Our products also allow our customers to insert advertising into broadcast and VOD content.

SeaChange serves an exciting global marketplace where multiscreen viewing is increasing, consumer device options are evolving rapidly, and viewer habits are shifting. The primary thrust of our business has been to enable the delivery of video assets in the evolving multiscreen television environment. Through acquisitions and partnerships, we have expanded our capabilities, products and services to address the delivery of content to devices other than television set-top boxes, namely PCs, tablets, smart phones and OTT streaming players. We believe that our strategy of expanding into adjacent product lines will position us to further support and maintain our existing service provider customer base. Providing our customers with more technologically advanced software platforms enables them to further reduce their infrastructure costs and improve reliability. Additionally, we believe we are well positioned to capitalize on new customers entering the multiscreen marketplace and increasingly serve adjacent markets, such as mobile and OTT. Our core technologies provide a foundation for products and services that can be deployed in next generation video delivery systems capable of increased levels of subscriber interactivity. We have received several awards for technological excellence, including three Emmy Awards for our pivotal roles in the growth of volume service provider businesses including VOD and multi-channel television advertising. Our achievements on behalf of certain customers have also received significant market recognition including, during fiscal year 2014, winning the Liberty Global Vendor Award for Best Product & Service Quality and the Cable Europe Innovation Award for cable operator Voo s multiscreen service launch.

On February 2, 2015, we acquired TLL, LLC (Timeline Labs), a California-based software-as-a-service (SaaS) company that enables local broadcasters, national news organizations and other media companies and brands to analyze social media messages in real-time, find and broadcast social trends, and measure viewing audience engagements across television, mobile and personal computers. Through its acquisition of Timeline Labs, SeaChange is a partner and technology provider for the NewCoin LLC (NewCoin) local television audience measurement venture with FOX Television Stations, Tribune Media and Univision. NewCoin s mission is to harness

the data-gathering power of currently available and emerging technologies in order to create a broader based measurement tool that will accurately measure audiences across the entire spectrum of linear and digital platforms.

In January 2015, we initiated a global restructuring plan to streamline our activities, primarily from an employee headcount reduction of 10%, now that our next generation software products have been brought to market and are being deployed around the globe. The reduction in workforce has been implemented immediately in the

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United States and, to comply with non-U.S. legal requirements, will be implemented on an international basis over the next several quarters. Once fully implemented, we expect this initiative to yield approximately \$11 million in annualized cost savings.

Products and Services

Our business is comprised of three product areas: multiscreen video, television advertising and video gateway software. Our revenue sources consist of product revenue from these areas, as well as related services.

Multiscreen Video

We offer our multiscreen video products under the following two deployment options, on-site software licenses and on a SaaS basis.

On-Site Software Licenses

In this model, revenue is derived from perpetual software license and annual maintenance and support fees, as well as associated professional services. This model includes the following:

SeaChange Adrenalin MultiScreen Television Platform. Adrenalin is a comprehensive software platform that enables service providers to manage, monetize and deliver a seamless viewing experience to subscribers across televisions, PCs, tablets, smart phones and other IP-enabled devices. Adrenalin is modular allowing our customers to gradually adopt new functionality and features to expand multiscreen television distribution capabilities. Adrenalin automates and streamlines functionality in four crucial areas:

Ingest of video content including custom workflow, transcoding, encryption and distribution;

Content management including data analysis and management of metadata;

Business management such as advertising placement, contract rights and subscriber entitlements, cloud-based monitoring and management and recommendation of social media applications; and

Publishing and purchasing, which allow content to be formatted for viewing on any device.

SeaChange Nitro Subscriber Experience Software. Our Nitro subscriber experience software gives service providers a customizable interface that personalizes the multi-platform subscriber experience and provides consistent presentation and navigation of linear, on-demand, OTT and time-shifted television. Nitro optimizes subscriber engagement and content promotions to ensure that the value of all content is fully realized on any consumer device.

SeaChange AssetFlow. In today's multiscreen viewing platform, a show, movie or advertisement and its associated metadata, such as poster, description and pricing, are reproduced with numerous variants to serve the unique requirements of multiple network types, consumer devices and geographies. At the point of content ingest, our AssetFlow software is used to receive, manage and publish content for on-demand viewing on televisions, tablets, PCs and other consumer devices. AssetFlow simplifies the increasingly complex tasks of movie and television program

asset tracking, metadata management, and overall content workflow.

SaaS Offering

In this model, we license our product offerings on a SaaS basis and our customers pay us on a monthly recurring basis based on the total number of subscriber lines deployed by the customer.

SeaChange Rave Premium OTT Video Platform. Our Rave premium OTT platform (Rave) offering provides a managed services offering for our customers. Rave enables live, time-shifted, pay-per-view and on-demand video services and storefront creation. Advanced content recommendations, discovery and social media are enabled through SeaChange's user experience and third-party applications. Rave includes services, tools and integrations for OTT content workflow, media management and analytics. Rave also enables video and interactive cross-device advertising throughout individual streams and user experiences. Advanced content promotion and monetization features include download to purchase and rent, subscription packaging and

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couponing. Through these features, Rave allows media companies and service providers to fully integrate with the connected consumer lifestyle and create a deeper audience relationship to project their brand and create pertinent, contextual promotions and advertising.

Television Advertising

SeaChange Infusion Advanced Advertising Platform. As more television content is served to multiple consumer devices, the ability to generate additional revenue by inserting targeted advertising on these devices becomes crucial to service providers seeking to offset content rights costs and reduce subscriber fees for viewing the content. Infusion enables service providers to maximize advertising revenue across multiscreen, broadcast, on-demand and OTT viewing and reach their audiences while viewers watch television on multiple devices. The platform incorporates demographic intelligence to target viewers by geography and personal preference, then engages the viewer through pre-rolls, mid-rolls, banners, overlays and click-action interactivity. Infusion scales to support service providers migration to consolidated regional and national advertising systems that are managed from increasingly web-centric and virtualized datacenters.

SeaChange Infusion AdPulse On-Demand Advertising Software. Service providers leverage Infusion AdPulse to capitalize on their VOD television services with ad placements that are dynamically targeted according to the content viewers select, as well as by geographic, demographic and viewing characteristics. Because the advertisements are tracked separately from the content, the data provided includes detailed advertisement viewing and trick-mode (fast-forward, rewind, and pause) usage leading to easier analysis of reach and effectiveness.

SeaChange AdFlow. AdFlow simplifies the ingest and preparation of content required to cost-effectively deliver multichannel or multiscreen advertising. It enables the range of advertisements to be ready for insertion, regardless of encoding formats, screen size, and the many other factors affecting today's linear, on-demand and multiscreen television operations. It also handles advertisement file processing, verification, transcoding operations and confirms payout for confident revenue booking.

Video Gateway Software

Nucleus. Nucleus ports to any set-top box, or other customer premises equipment hardware and system on a chip (SoC), and acts as a hub for all video distribution to any IP- connected device throughout the home, such as tablets, smart phones and game consoles.

SeaChange capitalized on open software and networking technologies to create Nucleus, a fully customizable foundation for rich multiscreen services running on the chipset and hardware. Nucleus enables the service providers to select the chipset, hardware and set-top box vendor of their choice. Nucleus extends providers' video services to a wide range of video consumer devices through its support for DLNA networking protocols, and enables them to enhance their overall offering by providing the framework for the introduction of new applications. Further, Nucleus leverages the industry Reference Design Kit, a technology standard that enables the video service provider community to take advantage of open technologies to more rapidly introduce and support service innovations.

Social Tools

SeaChange Timeline. SeaChange Timeline provides an end-to-end content management platform for media companies and brands to leverage the power of social content and conversations on a SaaS model. SeaChange Timeline simplifies the real-time editorial content and production process by offering the ability to discover social news, gather content relevant to an audience and present it with visualizations ready for video broadcast or the Internet.

Services

SeaChange offers comprehensive professional services and customer support for all of its products. We have developed extensive capabilities in systems integration, implementation and custom engineering. Our focus on,

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and expertise in video means that we often take on the role of primary integrator for increasingly complex multi-vendor deployments. We also offer managed services with advantages, including remote monitoring and proactive system maintenance, to help our customers quickly and confidently establish new on-demand and multiscreen services.

Strategy

Our goal is to strengthen our position as a leading global provider of multiscreen video by enabling service providers and content owners to increase revenue opportunities by delivering transformative multiscreen video products to their end subscribers. Key elements of our strategy include:

We intend to continue to provide to our existing base and new customers, industry-leading solutions through our focus on product innovation and substantial investment in research and development for our next generation software products and services;

We intend to accelerate adoption of our next generation products and services and time to market by promoting and expanding to adjacent markets such as mobile and OTT;

We intend to provide pre-packaged integrated solutions with the goal of better enabling new and existing customers to drive the adoption of the Rave and Timeline features and functions through a service offering hosted and/or managed by us;

We intend to continue to pursue acquisitions and collaborations which we believe will strengthen our industry leadership position, expand our geographic presence, or allow us to expand to new products or services, or enhance our existing ones;

We may enter into strategic relationships to help our customers address deficiencies in the their market space, such as our recent joint venture with FOX, Tribune Media and Univision to address the weaknesses in local television market audience measurement;

Although our initial sale with a service provider may be for a single screen and device, once a service provider deploys services using our Adrenalin platform, we believe we are well positioned to sell additional features to that service provider to help them expand the number of devices in their customers' households; and

Our customers are located worldwide and include top cable service providers. We believe we are well positioned to grow by adding customers in regions where we already have a strong presence and by expanding our geographic footprint in Asia Pacific and Latin America. In addition, we intend to penetrate more deeply into other markets such as mobile, telecommunications and media companies.

Research and Product Development

Our research and development costs were \$42.2 million in fiscal 2015, \$39.7 million in fiscal 2014 and \$38.7 million in fiscal 2013. We believe that our success will depend on our ability to develop and introduce timely new integrated solutions and enhancements to our existing products that meet changing customer requirements in our current and future customer base as well as new markets. We have made substantial investments in developing and bringing to market our next generation products. Our current research and development activities are focused on developing multiscreen television platforms, video gateway software and advertising solutions in the multiscreen video market, and integrating the solutions we currently offer. Our direct sales and marketing groups closely monitor changes in customer needs, changes in the marketplace and emerging industry standards to help us focus our research and development efforts to address our customers' needs, such as increasing average revenue per subscriber, lowering operating and capital costs and reducing customer churn. Our research and development efforts are performed in the United States at our Acton, Massachusetts headquarters as well as our sites in California; Oregon; Pennsylvania; and worldwide in Bangalore, India; Manila, Philippines; and Eindhoven, Netherlands.

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During fiscal 2015 we continued the focus of our research and development efforts on the next generation software platforms, which are vital to our customers' success. We achieved this by further increasing our investment in our software products for multiscreen video and video gateway software platforms, while reducing our investment in certain legacy product lines. As of January 31, 2015, we had a research and development staff of 296 employees.

Selling and Marketing

Our sales cycle tends to be long, in some instances twelve to twenty-four months, and purchase orders are typically in excess of one million dollars. As a result, it is sometimes difficult to predict what quarter or fiscal year our sales will occur. In light of the complexity of our video products, we primarily utilize a direct sales process. We sell and market our products worldwide through a direct sales organization, primarily conducted from our headquarters although we will use sales representatives deployed in different regions where we do not have a direct sales force. Working closely with customers to understand and define their needs enables us to obtain better information regarding market requirements, enhance our expertise in our customers' industries, and more effectively and precisely convey to customers how our solutions address their specific needs. As we recently announced, we have expanded our direct sales presence into Asia Pacific and Latin America.

We use several marketing programs to focus on our targeted markets to support the sale and distribution of our products. We also market certain of our products to systems integrators and value-added resellers. We attend and exhibit our products at a limited number of prominent industry trade shows and conferences and we present our technology at seminars and smaller conferences to promote the awareness of our products. We also publish articles in trade and technical journals. As of January 31, 2015, we had marketing and sales staff of 49 employees.

Manufacturing and Quality Control

Our manufacturing operation consists primarily of component and subassembly procurement, systems integration and final assembly, testing and quality control of the complete systems. As of January 31, 2015 we had a manufacturing staff of 11 employees.

Our Customers

We currently sell our products primarily to video service providers, such as cable system operators and telecommunications companies, as well as content providers. Our customer base is highly concentrated among a limited number of large service provider customers. A significant portion of our revenues in any given fiscal period have been derived from substantial orders placed by these large organizations. For the fiscal year ended January 31, 2015, Comcast and LGI each accounted for more than 10% of our total revenues.

We expect that we will continue to be dependent upon a limited number of customers for a significant portion of our revenues in the near future, even as we intend to penetrate new markets and customers. As a result of this customer concentration, our business, financial condition and results of operations could be materially adversely affected by the failure of anticipated orders to materialize and by deferrals or cancellations of orders as a result of changes in customer requirements or new product announcements or introductions. In addition, the concentration of customers may cause variations in revenue, expenses and operating results on a quarterly basis due to seasonality of orders, the timing and relative size of orders received and accepted during a fiscal quarter, or the timing and size of orders for which revenue recognition criteria have been satisfied during a fiscal quarter.

We do not believe that our backlog at any particular time is meaningful as an indicator of our future level of revenue for any particular period. Because of the requirements of particular customers, orders may require final acceptance

prior to revenue being recognized, resulting in the related revenues not being recognized in the ensuing quarter. Therefore, there is no direct correlation between the backlog at the end of any quarter and our total revenue for the following quarter or other periods.

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Competition

The markets in which we compete are characterized by intense competition, with a large number of suppliers providing different types of products to different segments of the markets. In new markets for our products, we compete principally based on price. In markets in which we have an established presence, we compete principally on the basis of the breadth of our products' features and benefits, including the flexibility, scalability, professional quality, ease of use, reliability and cost effectiveness of our products, and our reputation and the depth of our expertise, customer service and support. While we believe that we currently compete favorably overall with respect to these factors and that our ability to provide integrated solutions to manage and distribute digital video differentiates us from our competitors, in the future we may not be able to continue to compete successfully with respect to these factors.

In the market for multiscreen video, we compete with various larger companies offering video platforms and applications such as Cisco Systems, Inc., Arris Group Inc. (ARRIS), and Ericsson Inc. as well as in-house solutions. In our video gateway software market, we compete with system integrators and gateway software and applications vendors who offer proprietary software and hardware solutions. In the advertisement platform market, we generally compete with ARRIS. In the OTT market, we compete with online video platform providers such as Brightcove, Kaltura and Ooyala. We expect the competition in each of the markets in which we operate to intensify in the future as existing and new competitors with significant market presence and financial resources.

Many of our current and prospective competitors have significantly greater financial, technical, manufacturing, sales, marketing and other resources. As a result, these competitors may be able to devote greater resources to the development, promotion, sale and support of their products. Moreover, these companies may introduce additional products that are competitive with ours or enter into strategic relationships to offer complete solutions, and in the future our products may not be able to compete effectively with these products.

Proprietary Rights

Our success and our ability to compete are dependent, in part, upon our proprietary rights. We have been granted 31 patents worldwide, have several patents pending and have filed foreign patent applications related thereto for various technologies developed and used in our products. In addition, we rely on a combination of contractual rights, trademark laws, trade secrets and copyright laws to establish and protect our proprietary rights in our products. It is possible that in the future not all of these patent applications will be issued or that, if issued, the validity of these patents would not be upheld. It is also possible that the steps taken by us to protect our intellectual property will be inadequate to prevent misappropriation of our technology or that our competitors will independently develop technologies that are substantially equivalent or superior to our technology. In addition, the laws of some foreign countries in which our products are or may be distributed do not protect our proprietary rights to the same extent as do the laws of the United States. Currently, we are not party to intellectual property litigation, but we may be a party to litigation in the future to enforce our intellectual property rights or as a result of an allegation that we infringe others' intellectual property.

Employees

The table below represents the number of employees that we employ in different geographic areas across the world for the periods shown. We believe that our relations with our employees are good. None of our employees are represented by a collective bargaining agreement.

Country	January 31,		
	2015	2014	2013
United States	302	382	411
Philippines	161	150	143
Netherlands	137	111	97
Other international	103	80	71
Total employees by country	703	723	722

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The following is a list of our executive officers, their ages as of March 31, 2015 and their positions held with us:

Name	Age	Title
Jay A. Samit	54	Chief Executive Officer and Board member
Anthony C. Dias	48	Chief Financial Officer, Senior Vice President, Finance and Administration and Treasurer
David McEvoy	57	Senior Vice President and General Counsel and Secretary

Mr. Samit joined SeaChange as Chief Executive Officer (CEO) on October 20, 2014. Mr. Samit currently serves on the Board of Equal Earth Corporation and as an adjunct professor at the University of Southern California. Prior to joining SeaChange Mr. Samit was President at ooVoo, a social video chat service, from May 2011 to January 2013. Prior to that Mr. Samit served as CEO of SocialVibe (later renamed TrueX), a digital advertising technology company powering engagement for some of the world's top brands, from October 2009 to January 2011. Prior to that he held senior executive roles with Sony and EMI, where he spearheaded these companies' digital media efforts.

Mr. Dias joined the Company on December 3, 2007 as Vice President of Finance and Corporate Controller. He became Chief Financial Officer in September 2013. Prior to that, Mr. Dias served since June 2012 as Chief Accounting Officer. Prior to joining SeaChange, Mr. Dias served as Corporate Controller at LeMaitre Vascular, Inc. from October 2006 to November 2007. Prior to that Mr. Dias held various senior finance positions with Candela Corporation, Globalware, Inc. and Aldiscon, Inc. (later acquired by Logica). Mr. Dias is also a Certified Public Accountant.

Mr. McEvoy joined the Company on July 1, 2012 as Vice President and General Counsel. He became Senior Vice President and General Counsel on February 1, 2013. Prior to joining SeaChange, Mr. McEvoy was the Senior Vice President and General Counsel of Peoplefluent Inc. Mr. McEvoy was the Senior Vice President and General Counsel of Art Technology Group, Inc. (ATG) from September 2005 to March 2010. ATG was acquired by Oracle on January 5, 2011. Prior to joining ATG, Mr. McEvoy was the Group General Counsel of Gores Technology Group, a private equity firm. Mr. McEvoy has held various General Counsel and other executive level legal positions with several companies including Aprisma Inc., Anker Systems Ltd., VeriFone Inc., Mattel Interactive, Broderbund and The Learning Company.

Geographic Information

Geographic information is included in Part II, Item 7 of this Form 10-K under the heading *Management's Discussion and Analysis of Financial Condition and Results of Operations-Results of Operations* and in Note 11., *Segment Information, Significant Customers and Geographic Information*, to the consolidated financial statements located in Part II, Item 8, of this Form 10-K.

Available Information

SeaChange is subject to the informational requirements pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act). SeaChange files periodic reports, proxy statements and other information with the SEC. Such reports, proxy statements and other information may be obtained by visiting the

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Public Reference Room of the SEC at 100 F Street, N.E., Washington, DC 20549 or by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an internet site (<http://www.sec.gov>) that contains reports, proxy and information statements and other information regarding issuers that file electronically.

Financial and other information about SeaChange, including our Code of Ethics and Business Conduct and charters for our Audit Committee, Compensation Committee and Corporate Governance and Nominating

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Committee, is available on the Investor Relations section of our website at www.schange.com. We make available free of charge on our website our Form 10-K, Quarterly Reports on Form 10-Q (Form 10-Q), Current Reports on Form 8-K (Form 8-K) and amendments to those reports as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. The information contained on our web site is not incorporated by reference into this document and should not be considered a part of this Form 10-K. Our website address is included in this document as an inactive textual reference only.

Item 1A. RISK FACTORS

We wish to caution each reader of this Form 10-K to consider the following factors and other factors discussed herein and in other past reports, including but not limited to prior year Form 10-K and Form 10-Q reports filed with the SEC. Our business and results of operations could be materially affected by any of the following risks. The factors discussed herein are not exhaustive. Therefore, the factors contained herein should be read together with other reports that we file with the SEC from time to time, which may supplement, modify, supersede, or update the factors listed in this document.

Our business is dependent on customers continued spending on video systems and services. A reduction in spending by customers would adversely affect our business.

Our performance is dependent on customers continued spending for video systems and services. Spending for these systems and services is cyclical and can be curtailed or deferred on short notice. A variety of factors affect the amount of spending, and, therefore, our sales and profits, including:

general economic conditions;

customer specific financial or stock market conditions;

availability and cost of capital;

governmental regulation;

demand for services;

competition from other providers of video systems and services;

acceptance of new video systems and services by our customers; and

real or perceived trends or uncertainties in these factors.

Any reduction in spending by our customers would adversely affect our business. We continue to have limited visibility into the capital spending plans of our current and prospective customers. Fluctuations in our revenue can lead to even greater fluctuations in our operating results. Our planned expense levels depend in part on our expectations of future revenue. Our planned expenses include significant investments, particularly within our research and development organization, which we believe are necessary to continue to provide innovative solutions to meet our current and prospective customers' needs. As a result, it is difficult to forecast revenue and operating results. If our revenue and operating results are below the expectations of our investors and market analysts, it could cause a decline in the price of our common stock.

Our future success is dependent on the continued development of the multiscreen video and over the top (OTT) market and if these markets do not continue to develop, our business may not continue to grow.

A large portion of our anticipated revenue growth is expected to come from sales and services related to our multiscreen video and OTT products. However, these markets continue to develop as a commercial market, both within and outside North America. The potential size of these markets and the timing of their development are uncertain. The success of these markets require that video service providers continue to upgrade their cable networks to service and successfully market multiscreen video, OTT and similar services to their cable television

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subscribers. Some cable system operators, particularly outside of North America, are still in the early stages of commercial deployment of multiscreen video and OTT service to major residential cable markets. If cable system operators and telecommunications companies fail to make the capital expenditures necessary to upgrade their networks or determine that broad deployment of multiscreen video and OTT services is not viable as a business proposition or if our products cannot support a substantial number of subscribers while maintaining a high level of performance, our revenues will not grow as we have planned.

Our efforts to introduce a SaaS-based multiscreen service offering may either not succeed or impair our sale of on-site licensed offerings. The occurrence of either of which may adversely affect our financial condition and operating results.

We have been, and will continue to, devote considerable resources and allocate capital expenditures to growing our SaaS service offering revenue over the next several years. There can be no assurance that we will meet our revenue targets for this service and if we fail to achieve our revenue goals, our growth and operating results will be materially adversely affected. Additionally, new or existing customers may choose to purchase our SaaS services rather than our on-premise solutions. If our customers' purchases trend away from perpetual licenses toward our SaaS, or to the extent customers defer orders due to evaluation SaaS, our product revenues, and our timing of revenue generally, may be adversely affected, which could adversely affect our results of operations and financial condition.

If we are unable to successfully introduce new products or enhancements to existing products on a timely basis, our financial condition and operating results may be adversely affected by a decrease in sales of our products.

Because our business plan is based on technological development of new products and enhancements to our existing products, our future success is dependent on our successful introduction of these new products and enhancements on a timely basis. In the future we may experience difficulties that could delay or prevent the successful development, introduction and marketing of these and other new products and enhancements, or find that our new products and enhancements do not adequately meet the requirements of the marketplace or achieve market acceptance. Announcements of currently planned or other new product offerings may cause customers to defer purchasing our existing products. Moreover, despite testing by us and by current and potential customers, errors or failures may be found in our products, and, even if discovered, may not be successfully corrected in a timely manner. These errors or failures could cause delays in product introductions and acceptance, or require design modifications that could adversely affect our competitive position. Currently, we are focused on our next generation software products, including SeaChange Adrenalin, SeaChange Nucleus, SeaChange Infusion Advanced Advertising Platform and SeaChange Rave. Our inability to complete the development of these new products or enhancements on a timely basis or the failure of these new products or enhancements to achieve market acceptance could have a material adverse effect on our business, financial condition and results of operations in fiscal 2016 and in future periods.

We may be unsuccessful in our efforts to become a company that primarily provides software solutions.

Our efforts to become a company that primarily provides software solutions may result in a reduction in both the range of products and services we offer and in the range of our current and potential future customers. Each of these factors may increase the level of execution risk in our strategy, in that there may be increased variability in our revenues. If we are unsuccessful in this transition, our business, financial condition and results of operation may be adversely affected, and the market price of our common stock may decrease.

Our business is impacted by worldwide economic cycles, which are difficult to predict.

The global economy and financial markets experienced a severe downturn in recent years. The downturn stemmed from a multitude of factors, including, among other things, extreme volatility in security prices,

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diminished credit availability, concerns about inflation and deflation, rapid changes in foreign exchange rates, increased energy costs, decreased consumer confidence, rating downgrades of certain investments and declining valuations of others. These economic developments, the rate of recovery and the change in business spending resulting from these developments affect businesses such as ours and those of our customers and vendors in a number of ways that could result in unfavorable consequences to us. The continuation of the change in business spending from these events or further disruption and deterioration in economic conditions may reduce customer purchases of our products and services, thereby reducing our revenues and earnings. In addition, these events may, among other things, result in increased price competition for our products and services, increased risk in the collectability of our accounts receivable from our customers, increased risk in potential reserves for doubtful accounts and write-offs of accounts receivable, and higher operating costs as a percentage of revenues. We have taken actions to address the effects of the change in business spending and future economic cycles, including implementing cost control and cost reduction measures. It is possible that we may need to take further actions to control our cost structure and implement further cost reduction measures. We cannot predict whether these measures will be sufficient to offset certain of the negative trends that might affect our business.

We have taken and continue to take measures to address the variability in the market for our products and services, which could have long-term negative effects on our business or impact our ability to adequately address a rapid increase in customer demand.

We have taken and continue to take measures to address the variability in the market for our products and services, to increase average revenue per unit of our sales and to reduce our operating expenses, rationalize capital expenditure and minimize customer turnover. These measures include shifting more of our operations to lower cost regions by outsourcing and off-shoring, implementing cost reduction programs and reducing and rationalizing planned capital expenditures and expense budgets. We cannot ensure that the measures we have taken will not impair our ability to effectively develop and market products and services, to remain competitive in the industries in which we compete, to operate effectively, to operate profitably during slowdowns or to effectively meet a rapid increase in customer demand. These measures may have long-term negative effects on our business by reducing our pool of technical talent, decreasing or slowing improvements in our products and services, making it more difficult to hire and retain talented individuals and to quickly respond to customers or competitors in an upward cycle.

Because our customer base is highly concentrated among a limited number of large customers, a change in demand by, a return of product by or the failure to satisfy revenue acceptance criteria in a given quarter by one or more of these customers, could have a material adverse effect on our business, financial condition and results of operations.

Our customer base is highly concentrated among a limited number of large customers, and, therefore, a limited number of customers account for a significant percentage of our revenues in any fiscal period. We generally do not have written agreements that require customers to purchase fixed minimum quantities of our products. Our sales to specific customers tend to vary significantly from year to year and from quarter to quarter depending upon these customers' budgets for capital expenditures and our new product introductions. We believe that a significant amount of our revenues will continue to be derived from a limited number of large customers in the future. The loss of, reduced demand for products or related services by, return of a product previously purchased by any of our major customers or the failure of revenue acceptance criteria to have been satisfied in a given fiscal quarter, could materially and adversely affect, either in a particular quarter or on a more long-term basis, our business, financial condition and results of operations.

Consolidations in the television service providers industry could result in delays or reductions in purchases of products, which would have a material adverse effect on our business.

The television service providers industry has historically experienced, and continues to experience, the consolidation of many industry participants. For example, in the first half of calendar 2014, Comcast announced

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its proposed acquisition of Time Warner Cable and AT&T announced its proposed acquisition of DIRECTV and in February 2015, Verizon Communications Inc. announced that it is selling certain wireline businesses to Frontier Communications Corp. When consolidations occur, it is possible that the acquirer will not continue using the same suppliers, possibly resulting in an immediate or future elimination of sales opportunities for us or our competitors. Even if sales are not reduced, consolidation can also result in pressure from customers for lower prices or better terms, reflecting the increase in the total volume of products purchased or the elimination of a price differential between the acquiring customer and the company acquired. Consolidations also could result in delays in purchasing decisions by the affected companies prior to completion of the transaction and by the merged businesses. The purchasing decisions of the merged companies could have a material adverse effect on our business.

Cancellation or deferral of purchases of our products or final customer acceptance, or the return of previously purchased products could cause a substantial variation in our operating results, resulting in a decrease in the market price of our common stock and making period-to-period comparisons of our operating results less meaningful.

We derive a substantial portion of our revenues from purchase orders that exceed one million dollars in value. Therefore, any significant cancellation or deferral of purchases of our products or receiving final customer acceptance could result in a substantial variation in our operating results in any particular quarter due to the resulting decrease in revenue and gross margin. In addition, to the extent significant sales occur earlier than expected, operating results for subsequent quarters may be adversely affected because our operating costs and expenses are based, in part, on our expectations of future revenues, and we may be unable to adjust spending in a timely manner to compensate for any revenue shortfall. Because of these factors, in some future quarter our operating results may be below guidance that we may issue or the expectations of public market analysts and investors, any of which may adversely affect the market price of our common stock. In addition, these factors may make period-to-period comparisons of our operating results less meaningful.

Due to the lengthy sales cycle involved in the sale of our products, our quarterly results may vary and should not be relied on as an indication of future performance.

Our next generation software products and related services are relatively complex and their purchase generally involves a significant commitment of capital, with attendant delays frequently associated with large capital expenditures and implementation procedures within an organization. Moreover, the purchase of these products typically requires coordination and agreement among a potential customer's corporate headquarters and its regional and local operations. For these and other reasons, the sales cycle associated with the purchase of our next generation software products and services is typically lengthy and subject to a number of significant risks, including customers budgetary constraints and internal acceptance reviews, over which we have little or no control. Based upon all of the foregoing, we believe that our quarterly revenues and operating results are likely to vary significantly in the future, that period-to-period comparisons of our results of operations are not necessarily meaningful and that these comparisons should not be relied upon as indications of future performance.

If there were a decline in demand or average selling prices for our products, our revenues and operating results would be materially affected.

We expect our next generation software product lines to account for a significant portion of our revenues. Accordingly, a decline in demand or average selling prices for these products in the foreseeable future, whether as a result of new product introductions by others, price competition, technological change, inability to enhance the products in a timely fashion, or otherwise, could have a material adverse effect on our business, financial condition and results of operations.

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We must manage product transitions successfully in order to remain competitive.

The introduction of a new product or product line is a complex task, involving significant expenditures in research and development, training, promotion and sales channel development. However, we cannot assure that we will be able to execute product transitions in an efficient manner or that product transitions will be executed without harming our operating results. Failure to develop products with required features and performance levels or any delay in bringing a new product to market could significantly reduce our revenues and harm our competitive position.

We may fail to achieve our financial forecasts due to inaccurate sales forecasts or other factors.

Our revenues are difficult to forecast, and as a result, our quarterly operating results can fluctuate substantially. We use a pipeline system, a common industry practice, to forecast sales and trends in our business. Our sales personnel monitor the status of all proposals and estimate when a customer will make a purchase decision and the dollar amount of the sale. These estimates are aggregated periodically to generate a sales pipeline. Our pipeline estimates can prove to be unreliable both in a particular quarter and over a longer period of time, in part because the conversion rate or closure rate of the pipeline into contracts can be very difficult to estimate. A reduction in the conversion rate, or in the pipeline itself, could cause us to plan or budget incorrectly and adversely affect our business or results of operations. In particular, a slowdown in capital spending or economic conditions generally can unexpectedly reduce the conversion rate in particular periods as purchasing decisions are delayed, reduced in amounts or cancelled. The conversion rate can also be affected by the tendency of some of our customers to wait until the end of a fiscal period in the hope of obtaining more favorable terms, which can also impede our ability to negotiate, execute and deliver upon these contracts in a timely manner. In addition, for our new product offerings, including those acquired through our Timeline Labs acquisition, we have limited ability to predict how their pipelines will convert into sales or revenues. Conversion rates for new product offerings are often variable as product acceptance often takes longer than anticipated and conversion rates for products acquired through acquisition may be quite different from the acquired companies' historical conversion rates, including from changes in our business practices that we implement with our newly acquired companies that may affect customer behavior.

Because a significant portion of our cost structure is largely fixed in the short-term, revenue shortfalls tend to have a disproportionately negative impact on our profitability. The number of large new software licenses transactions increases the risk of fluctuations in our quarterly results because a delay in even a small number of these transactions could cause our quarterly revenues and profitability to fall significantly short of our predictions.

If we are unable to manage our growth and the related expansion in our operations effectively, our business may be harmed through a diminished ability to monitor and control effectively our operations, and a decrease in the quality of work and innovation of our employees.

Our ability to successfully offer new products and services and implement our business plan in a rapidly evolving market requires effective planning and management. We are also continuing to transition towards greater reliance on our software products and services for a significant portion of our total revenue. In light of the growing complexities in managing our expanding portfolio of products and services, our anticipated future operations may continue to strain our operational and administrative resources. To manage future growth effectively, we must continue to improve our operational controls and internal controls over financial reporting, integrate new personnel and the businesses we have acquired, or will acquire, and manage our expanding international operations. A failure to manage our growth may harm our business through a decreased ability to monitor and control effectively our operations, and a decrease in the quality of work and innovation of our employees upon which our business is dependent.

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Because our business is susceptible to risks associated with international operations, we may not be able to maintain or increase international sales of our products and services.

Our international operations are expected to continue to account for a significant portion of our business in the foreseeable future. However, in the future we may be unable to maintain or increase international sales of our products and services. Our international operations are subject to a variety of risks, including:

difficulties in establishing and managing international distribution channels;

difficulty in staffing and managing foreign operations;

difficulties in selling, servicing and supporting overseas products and services and in translating products and services into foreign languages;

the uncertainty of laws and enforcement in certain countries relating to the protection of intellectual property;

fluctuations in currency exchange rates;

multiple and possibly overlapping tax structures;

negative tax consequences such as withholding taxes and employer payroll taxes;

differences in labor laws and regulations affecting our ability to hire and retain employees;

business and operational disruptions or delays caused by political, social and economic instability and unrest, including risks related to terrorist activity;

changes in economic policies by foreign governments, including the imposition and potential continued expansion of economic sanctions by the U.S. and the European Union on the Russian Federation;

the burden of complying with a wide variety of foreign laws, treaties and technical standards; and

growth and stability of the economy or political changes in international markets.

The effect of one or more of these international risks could have a material and adverse effect on our business, financial condition, operating results and cash flow.

We are subject to the Foreign Corrupt Practices Act (FCPA), and our failure to comply could result in penalties which could harm our reputation, business, and financial condition.

We are subject to the FCPA, which generally prohibits companies and their intermediaries from making improper payments to foreign officials for the purpose of obtaining or keeping business. The FCPA also requires companies to maintain adequate record-keeping and internal accounting practices to accurately reflect the transactions of the Company. Under the FCPA, U.S. companies may be held liable for actions taken by their strategic or local partners or representatives. The FCPA and similar laws in other countries can impose civil and criminal penalties for violations.

If we do not properly implement practices and controls with respect to compliance with the FCPA and similar laws, or if we fail to enforce those practices and controls properly, we may be subject to regulatory sanctions, including administrative costs related to governmental and internal investigations, civil and criminal penalties, injunctions and restrictions on our business activities, all of which could harm our reputation, business and financial condition.

We are exposed to fluctuations in currency exchange rates that could negatively impact our financial results and cash flows.

Because a significant portion of our business is conducted outside the United States, we face exposure to adverse movements in foreign currency exchange rates. These exposures may change over time as business practices

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evolve, and they could have a material adverse impact on our financial results and cash flows. An increase in the value of the U.S. dollar could increase the real cost to our customers of our products in those markets outside the United States where we often sell in dollars, and a weakened dollar could increase local currency operating costs. In preparing our consolidated financial statements, certain financial information is required to be translated from foreign currencies to the U.S. dollar using either the spot rate or the weighted-average exchange rate. If the U.S. dollar weakens or strengthens relative to applicable local currencies, there is a risk our reported sales, operating expenses, and net income could significantly fluctuate. We are not able to predict the degree of exchange rate fluctuations, nor can we estimate the effect any future fluctuations may have upon our future operations. For example, the exchange rate of the U.S. dollar to foreign currency has strengthened significantly of late, which could make the price of our products and services outside the United States less competitive, reducing our sales and negatively impacting our financial results.

Our ability to compete could be jeopardized if we are unable to protect our intellectual property rights from third-party challenges.

Our success and ability to compete depends upon our ability to protect our proprietary technology that is incorporated into our products. We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. Although we have issued patents, we cannot assure that any additional patents will be issued or that the issued patents will not be invalidated. We also enter into confidentiality or license agreements with our employees, consultants and corporate partners, and control access to and distribution of our software, documentation and other proprietary information. Despite these precautions, it may be possible for a third-party to copy or otherwise misappropriate and use our products or technology without authorization, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States. We may need to resort to litigation in the future to enforce our intellectual property rights, to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. If competitors are able to use our technology, our ability to compete effectively could be harmed.

We have been and in the future could become subject to litigation regarding intellectual property rights, which could seriously harm our business and require us to incur significant legal costs to defend our intellectual property rights.

The industry in which we operate is characterized by vigorous protection and pursuit of intellectual property rights or positions, which on occasion, have resulted in significant and often protracted litigation. We have from time to time received, and may in the future receive, communications from third parties asserting infringements on patent or other intellectual property rights covering our products or processes. We may be a party to litigation in the future to enforce our intellectual property rights or as a result of an allegation that we infringe others' intellectual property. Any parties asserting that our products infringe upon their proprietary rights would force us to defend ourselves and possibly our customers or manufacturers against the alleged infringement, as many of our commercial agreements require us to defend and/or indemnify the other party against intellectual property infringement claims brought by a third party with respect to our products. We have received certain claims for indemnification from customers but have not been made party to any litigation involving intellectual property infringement claims as a result. These claims and any resulting lawsuit, if successful, could subject us to significant liability for damages and invalidation of our proprietary rights. This possibility of multiple damages serves to increase the incentive for plaintiffs to bring such litigation. In addition, these lawsuits, regardless of their success, would likely be time-consuming and expensive to resolve and would divert management time and attention away from our operations. Although we carry general liability insurance, our insurance may not cover potential claims of this type or may not be adequate to indemnify us for all liability that may be imposed. In addition, any potential intellectual property litigation also could force us to stop selling, incorporating or using the products that use the infringed intellectual property or obtain from the owner of the infringed intellectual property right a license to sell or use the relevant technology, although this license may not be available on reasonable

terms, or at all, or redesign those products that use the infringed intellectual property. If we are forced to take any of the foregoing actions, our business may be seriously harmed.

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If content providers limit the scope of content licensed for use in the digital VOD and OTT market, our business, financial condition and results of operations could be negatively affected because the potential market for our products would be more limited than we currently believe and have communicated to the financial markets.

The success of the multiscreen video market is contingent on content providers permitting their content to be licensed for use in this market. Content providers may, due to concerns regarding either or both marketing and illegal duplication of the content, limit the extent to which they provide content to their subscribers. A limitation of content for the VOD and OTT market would indirectly limit the market for our products which are used in connection with that market.

If we are not able to obtain necessary licenses, services or distribution rights for third-party technology at acceptable prices, or at all, our products could become obsolete or we may not be able to deliver certain product offerings.

We have incorporated third-party licensed technology into our current products and our product lines. From time to time, we may be required to license additional technology or obtain services from third parties to develop new products or product enhancements or to provide specific solutions. Third-party providers may not be available or continue to be available to us on commercially reasonable terms. The inability to maintain or re-license any third-party products required in our current products or to obtain any new third-party licenses and services necessary to develop new products and product enhancements or provide specific solutions could require us to obtain substitute technology of lower quality or performance standards or at greater cost. Such inability could delay or prevent us from making these products or services, which could seriously harm the competitiveness of our solutions.

We may also incorporate open source software into our products. Although we monitor our use of open source closely, the terms of many open source licenses have not been interpreted by U.S. courts, and there is a risk that such licenses could be construed in a manner that could impose unanticipated conditions or restrictions on our ability to commercialize our products. We could also be subject to similar conditions or restrictions should there be any changes in the licensing terms of the open source software incorporated into our products. In either event, we could be required to seek licenses from third parties in order to continue offering our products, to re-engineer our products or to discontinue the sale of our products in the event re-engineering cannot be accomplished on a timely or successful basis, any of which could adversely affect our business, operating results and financial condition.

If we are unable to successfully compete in our marketplace, our financial condition and operating results may be adversely affected.

We currently compete against large companies offering video software solutions. To the extent the products developed are competitive with and not complementary to our products, they may be more cost effective than our solutions, which could result in cable system operators and telecommunications companies discontinuing their purchases of our on-demand products. Due to the rapidly evolving markets in which we compete, additional competitors with significant market presence and financial resources, such as in-house solutions and online video platforms, may enter those markets, thereby further intensifying competition. Increased competition could result in price reductions, cancellations of purchase orders, losses of business with current customers to competitors, and loss of market share which would adversely affect our business, financial condition and results of operations. Many of our current and potential competitors have greater financial, selling and marketing, technical and other resources than we do. They may be in better position to withstand any significant reduction in capital spending by customers in our markets and may not be as susceptible to downturns in a particular market. Moreover, our competitors may also foresee the course of market developments more accurately than we do. Although we believe that we have certain

technological and other advantages over our competitors, realizing and maintaining these advantages will require a continued high level of investment by us in research and product development, marketing and customer service and support. In the future we may not have sufficient resources to continue to

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make these investments or to make the technological advances necessary to compete successfully with our existing competitors or with new competitors. If we are unable to compete effectively, our business, prospects, financial condition and operating results would be materially adversely affected because of the difference in our operating results from the assumptions on which our business model is based.

If we fail to respond to rapidly changing technologies related to multiscreen video, our business, financial condition and results of operations would be materially adversely affected because the competitive advantage of our products and services relative to those of our competitors would decrease.

The markets for our products are characterized by rapidly changing technology, evolving industry standards and frequent new product introductions and enhancements. Future technological advances in the television and video industries may result in the availability of new products or services that could compete with the solutions provided by us or reduce the cost of existing products or services, any of which could enable our existing or potential customers to fulfill their video needs better and more cost efficiently than with our products. Our future success will depend on our ability to enhance our existing video products, including the development of new applications for our technology, and to develop and introduce new products to meet and adapt to changing customer requirements and emerging technologies such as the OTT market. In the future, we may not be successful in enhancing our video products or developing and marketing new products which satisfy customer needs or achieve market acceptance. In addition, there may be services, products or technologies developed by others that render our products or technologies uncompetitive, unmarketable or obsolete, or announcements of currently planned or other new product offerings either by us or our competitors that cause customers to defer or fail to purchase our existing solutions.

We may not fully realize the benefits of our completed acquisitions or it may take longer than we anticipate for us to achieve those benefits. Future acquisitions may be difficult to integrate, disrupt our business, dilute stockholder value or divert management attention.

As part of our business strategy, we have acquired and may in the future seek to acquire or invest in new businesses, products or technologies that we believe could complement or expand our business, augment our market coverage, enhance our technical capabilities or otherwise offer growth opportunities such as our acquisition of Timeline Labs on February 2, 2015. Acquisitions could create risks for us, including:

difficulties in assimilation of acquired personnel, operations, technologies or products which may affect our ability to develop new products and services and compete in our rapidly changing marketplace due to a resulting decrease in the quality of work and innovation of our employees upon which our business is dependent;

delays in realizing, or failure to realize, the anticipated benefits of an acquisition;

adverse effects on the business relationships with pre-existing suppliers and customers of both companies. This may be of particular importance to our business because we sell our products to a limited number of large customers, we purchase certain components used in manufacturing our products from sole suppliers and we use a limited number of third-party manufacturers to manufacture our product; and

uncertainty among current and prospective employees regarding their future roles with our company, which might adversely affect our ability to retain, recruit and motivate key personnel.

Acquisitions or divestitures may adversely affect our financial condition.

We acquired Timeline Labs on February 2, 2015 to supplement and expand our product offerings. In the future, we could acquire additional products, technologies or businesses, or enter into joint venture arrangements, for the purpose of complementing or expanding our business. Negotiation of potential acquisitions, divestitures or joint ventures and our integration or transfer of acquired or divested products, technologies or businesses, could divert management's time and resources.

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As part of our strategy for growth, we may continue to explore acquisitions, divestitures, or strategic alliances, which may not be completed or may not be ultimately beneficial to us.

Acquisitions or divestitures may pose risks to our operations, including:

problems and increased costs in connection with the integration or divestiture of the personnel, operations, technologies, or products of the acquired or divested businesses;

unanticipated costs;

potential disruption of our business and the diversion of management's attention from our core business during the acquisition process;

inability to make planned divestitures of businesses on favorable terms in a timely manner or at all;

acquired assets becoming impaired as a result of technical advancements or worse-than-expected performance by the acquired company; and entering markets in which we have no, or limited, prior experience.

Additionally, in connection with any acquisitions or investments we could:

issue stock that would dilute our existing stockholders' ownership percentages, such as we agreed to do with our Timeline Labs acquisition;

incur debt and assume liabilities;

record contingent liabilities estimated for potential earnouts based on achieving financial targets;

obtain financing on unfavorable terms;

incur amortization expenses related to acquired intangible assets or incur large and immediate write-offs;

incur large expenditures related to office closures of the acquired companies, including costs relating to the termination of employees and facility and leasehold improvement charges resulting from our having to vacate the acquired companies' premises; and

reduce the cash that would otherwise be available to fund operations or for other purposes.

The performance of the companies in which we have made and may in the future make equity investments could have a material adverse effect on our financial condition and results of operations.

We have made non-controlling equity investments in complementary companies and we may in the future make additional investments. These investments may require additional capital and may not generate the expected rate of return that we believed possible at the time of making the investment. This may adversely affect our financial condition or results of operations. Also, investments in development-stage companies may generate other than temporary declines in fair value of our investment that would result in impairment charges.

If our indefinite-lived or other intangible assets become impaired, we may be required to record a significant charge to earnings.

Under accounting principles generally accepted in the United States (U.S. GAAP), we review our intangible assets, including goodwill, for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Indefinite-lived assets are required to be tested for impairment at least annually. Factors that may be considered a change in circumstances indicating that the carrying value of our indefinite-lived assets or other intangible assets may not be recoverable include declines in our stock price and market capitalization, or decreased future cash flows projections. Our valuation methodology for assessing impairment requires management to make judgments and assumptions based on projections of future operating performance. We

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operate in highly competitive environments and projections of future operating results and cash flows may vary significantly from actual results. We may be required to record a significant noncash charge to earnings in our financial statements during the period in which any impairment of our indefinite-lived assets or other intangible assets is determined.

We may experience risks in our investments due to changes in the market, which could adversely affect the value or liquidity of our investments.

We maintain a portfolio of marketable securities in a variety of instruments which may include commercial paper, certificates of deposit, money market funds and government debt securities. These investments are subject to general credit, liquidity, market, and interest rate risks. As a result, we may experience a reduction in value or loss of liquidity of our investments. These market risks associated with our investment portfolio may have a negative adverse effect on our results of operations, liquidity and financial condition.

The success of our business model could be influenced by changes in the regulatory environment, such as changes that either would limit capital expenditures by television, cable or telecommunications operators or reverse the trend towards deregulation in the industries in which we compete.

The telecommunications and television industries are subject to extensive regulation which may limit the growth of our business, both in the United States and other countries. The growth of our business internationally is dependent in part on deregulation of the telecommunications industry abroad, similar to that which has occurred in the United States, and the timing and magnitude of this growth, which is uncertain. Video service providers are subject to extensive government regulation by the Federal Communications Commission and other federal, state and international regulatory agencies. These regulations could have the effect of limiting capital expenditures by video service providers and thus could have a material adverse effect on our business, financial condition and results of operations. The enactment by federal, state or international governments of new laws or regulations, changes in the interpretation of existing regulations or a reversal of the trend toward deregulation in these industries could adversely affect our customers, and thereby materially adversely affect our business, financial condition and results of operations.

We may not be able to hire and retain highly skilled employees, which could affect our ability to compete effectively because our business is technology-based.

Our success depends to a significant degree upon the continued contributions of our key personnel, many of whom would be difficult to replace. We believe that our future success will also depend in large part upon our ability to attract and retain highly skilled managerial, engineering, customer service, selling and marketing, finance, administrative and manufacturing personnel, as our business is technology-based. Because competition for these personnel is intense, we may not be able to attract and retain qualified personnel in the future. The loss of the services of any of the key personnel, the integration of new personnel, the inability to attract or retain qualified personnel in the future or delays in hiring required personnel, particularly software engineers and sales personnel could have a material adverse effect on our business, financial condition and results of operations because our business is technology-based.

We face significant risks to our business when we engage in the outsourcing of engineering work, including outsourcing of software work overseas, which, if not properly managed, could result in the loss of valuable intellectual property and increased costs due to inefficient and poor work product, which could harm our business, including our financial results, reputation, and brand.

We may, from time-to-time, outsource engineering work related to the design and development of our products, typically to save money and gain access to additional engineering resources. We have worked, and expect to work in the future, with companies located in jurisdictions outside of the United States, including, but not limited to India, Poland and the Philippines. We have limited experience in the outsourcing of engineering and other

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work to third-parties located internationally that operate under different laws and regulations than those in the United States. If we are unable to properly manage and oversee the outsourcing of this engineering and other work related to our products, we could suffer the loss of valuable intellectual property, or the loss of the ability to claim such intellectual property, including patents and trade names. Additionally, instead of saving money, we could in fact incur significant additional costs as a result of inefficient engineering services and poor work product. As a result, our business would be harmed, including our financial results, reputation, and brand.

We may have additional tax liabilities.

We are subject to income taxes in both the United States and numerous foreign jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. We are regularly under audit by various tax jurisdictions. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation could be materially different from our historical income tax provisions and accruals. The results of an audit or litigation could have a material effect on our income tax provision, net income, or cash flows in the period or periods for which that determination is made. In addition, we are subject to sales, use and similar taxes in many countries, jurisdictions and provinces, including those states in the United States where we maintain a physical presence or have a substantial nexus. These taxing regimes are complex. For example, in the United States, each state and local taxing authority has its own interpretation of what constitutes a sufficient physical presence or nexus to require the collection and remittance of these taxes. Similarly, each state and local taxing authority has its own rules regarding the applicability of sales tax by customer or product type.

In September 2013, we received an audit notification from the Internal Revenue Service (IRS) requesting materials relating to our 2009 through 2011 federal tax return. As of January 31, 2015, we continue to provide information relating to the audit and have not received or agreed upon any final adjustments from the IRS.

If our security measures are breached and unauthorized access is obtained to a customer's data or our data on our systems, our service may be perceived as not being secure, customers may curtail or stop using our service and we may incur significant legal and financial exposure and liabilities.

Our service involves the transmission of customers' proprietary information and security breaches could expose us to a risk of loss of this information or a network disruption, which may result in litigation and possible liability. These security measures may be breached as a result of third-party action, including intentional misconduct by computer hackers, employee error, malfeasance or otherwise and result in unauthorized publication of our confidential business or proprietary information, cause an interruption in our operations, result in the unauthorized release of customer or employee data, result in a violation of privacy or other laws, expose us to a risk of litigation or damage our reputation, which could harm our business and operating results. Additionally, third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information in order to gain access to our customers' data or our data or IT systems. Because the techniques used to obtain unauthorized access, or to sabotage systems, change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. In addition, our customers may authorize third-party technology providers to access their customer data. Because we do not control our customers and third-party technology providers, or the processing of such data by third-party technology providers, we cannot ensure the integrity or security of such transmissions or processing. Malicious third-parties may also conduct attacks designed to temporarily deny customers access to our services. Any security breach could result in a loss of confidence in the security of our service, damage our reputation, negatively impact our future sales, disrupt our business and lead to legal liability. While we believe that we have taken appropriate security measures to minimize these risks to our data and information systems, there can be no assurance that our efforts will

prevent breakdowns or breaches in our systems that could adversely affect our business.

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Recently reported hacking attacks on government and commercial computer systems raise the risks that such an attack may compromise, in a material respect, one or more of our computer systems and permit hackers access to our proprietary information and data. If such an attack does, in fact, allow access to or theft of our proprietary information or data, our business, operating results and reputation could be materially and adversely affected.

Interruptions or delays in service from our third-party data center hosting facilities could impair the delivery of our service and harm our business.

For our customers buying our SaaS product offering, we use third-party data center hosting facilities located in the United States and the United Kingdom. Any damage to, or failure of, our systems generally could result in interruptions in our service. Interruptions in our service may reduce our revenue, cause us to issue credits or pay penalties, cause customers to terminate their subscriptions and adversely affect our attrition rates and our ability to attract new customers. Our business will also be harmed if our customers and potential customers believe our service is unreliable. We do not control the operation of any of these facilities, and they are vulnerable to damage or interruption from earthquakes, floods, fires, power loss, telecommunications failures and similar events. They may also be subject to break-ins, sabotage, intentional acts of vandalism and similar misconduct. Despite precautions taken at these facilities, the occurrence of a natural disaster or an act of terrorism, a decision to close the facilities without adequate notice or other unanticipated problems at these facilities could result in lengthy interruptions in our service. Even with the disaster recovery arrangements, our service could be interrupted.

We recently implemented a restructuring program, which could have a material negative impact on our business.

To increase strategic focus and operational efficiency, at the end of January 2015, we implemented a restructuring program that will affect approximately 100 full-time positions. We anticipate completing the majority of the activities related to our restructuring program over the next several quarters. We may incur additional restructuring costs or not realize the expected benefits of these new initiatives. Further, we could experience delays, business disruptions, decreased productivity, unanticipated employee turnover and increased litigation related costs in connection with the restructuring and other efficiency improvement activities, and there can be no assurance that our estimates of the savings achievable by the restructuring will be realized. As a result, our restructuring and our related cost reduction activities could have an adverse impact on our financial condition or results of operations.

Our stock price may be volatile and an investment in our stock may decline.

Historically, the market for technology stocks has been extremely volatile. Our common stock has experienced, and may continue to experience, substantial price volatility. The occurrence of any one or more of the factors noted above could cause the market price of our common stock to fluctuate. The stock market in general, and The NASDAQ Global Select Market (NASDAQ) and technology companies in particular, have experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of such companies. These broad market and industry factors may materially adversely affect the market price of our common stock, regardless of our actual operating performance. In these circumstances, investors may be unable to sell their shares of our common stock at or above their purchase price over the short-term, or at all. In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted against such companies.

Securities analysts may not publish favorable research or reports about our business or may publish no information which could cause our stock price or trading volume to decline.

The trading market for our common stock is influenced by the research and reports industry or financial analysts publish about us and our business. We do not control these analysts. If any of the analysts who cover us issue an adverse opinion regarding our stock price, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports covering us, we could lose visibility in the market, which in turn could cause our stock price or trade volume to decline.

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We utilize non-GAAP reporting in our quarterly earnings press releases.

We publish non-GAAP financial measures in our quarterly earnings press releases along with a reconciliation of non-GAAP financial measures to those measures compiled in accordance with accounting principles generally accepted in the U.S. GAAP. The reconciling items have adjusted U.S. GAAP net (loss) income and U.S. GAAP (loss) earnings per share for certain non-cash, non-operating or non-recurring items and are described in detail in each such quarterly earnings press release. We believe that this presentation may be more meaningful to investors in analyzing the results of operations and income generation as this is how our business is managed. The market price of our stock may fluctuate based on future non-GAAP results if investors base their investment decisions upon such non-GAAP financial measures. If we decide to curtail use of non-GAAP financial measures in our quarterly earnings press releases, the market price of our stock could be affected if investors analyze our performance in a different manner.

Any weaknesses identified in our system of internal controls by us and our independent registered public accounting firm pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 could have an adverse effect on our business.

Section 404 of the Sarbanes-Oxley Act of 2002 requires that companies evaluate and report on their systems of internal control over financial reporting. In addition, our independent registered public accounting firm must report on its evaluation of those controls. In future periods, we may identify deficiencies, including as a result of the loss of the services of one or more of our key personnel, in our system of internal controls over financial reporting that may require remediation. There can be no assurances that any such future deficiencies identified may not be significant deficiencies or material weaknesses that would be required to be reported in future periods.

Because we purchase certain material components used in manufacturing our products from sole suppliers and we use a limited number of third-party manufacturers to manufacture our products, our business, financial condition and results of operations could be materially adversely affected by a failure of these suppliers or manufacturers.

We rely on a limited number of third parties who manufacture certain components used in our products. We may experience quality control problems, where products did not meet specifications or were damaged in shipping, and delays in the receipt of these components. These risks could be heightened during a substantial economic slowdown or if a sole supplier were adversely affected by a natural disaster because our suppliers are more likely to experience adverse changes in their financial condition and operations during such a period. While we believe that there are alternative suppliers available for these components, we believe that the procurement of these components from alternative suppliers could take a significant amount of time. In addition, these alternative components may not be functionally equivalent or may be unavailable on a timely basis or on similar terms. The inability to obtain sufficient key components as required, or to develop alternative sources if and as required in the future, could result in delays or reductions in product shipments which, in turn, could have a material adverse effect on our business, financial condition and results of operations. While to date there has been suitable third-party manufacturing capacity readily available at acceptable quality levels, in the future there may not be manufacturers that are able to meet our future volume or quality requirements at a price that is favorable to us. Any financial, operational, production or quality assurance difficulties experienced by these third-party manufacturers that result in a reduction or interruption in supply to us could have a material adverse effect on our business, financial condition and results of operations.

Regulations related to conflict minerals could adversely impact our business.

The Dodd-Frank Wall Street Reform and Consumer Protection Act contains provisions to improve transparency and accountability concerning the supply of certain minerals, known as conflict minerals. As a result, the SEC adopted

annual disclosure and reporting requirements for those companies who use conflict minerals mined from the DRC and adjoining countries in their products. These regulations may require due diligence efforts by the Company each year with disclosure requirements due annually on May 31st. There are costs associated with

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complying with these disclosure requirements, including due diligence to determine the sources of conflict minerals used in our products and other potential changes to products, processes or sources of supply as a consequence of such verification activities. Even though we are not aware of any conflict minerals in our products, the implementation of these rules could adversely affect the sourcing, supply and pricing of materials used in our products in the future. As there may be only a limited number of suppliers offering conflict free conflict minerals, we cannot be sure that we will be able to obtain necessary materials from such suppliers in sufficient quantities or at competitive prices. Also, we may face adverse effects to our reputation if we determine that certain of our products contain minerals not determined to be conflict free or if we are unable to sufficiently verify the origins for all conflict minerals used in our products through the procedures we may implement.

As a Delaware corporation, we are subject to certain Delaware anti-takeover provisions.

As a Delaware corporation, we are subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation Law, which may, unless certain criteria are met, prohibit large stockholders, in particular those owning 15% or more of the voting rights of our common stock, from merging or combining with us for a practical period of time. Any provision of our certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control of SeaChange could limit the opportunity of our stockholders to receive a premium for their shares of SeaChange common stock and also could affect the price that some investors are willing to pay for our common stock.

Changes in financial accounting standards may cause adverse unexpected revenue fluctuations and affect our reported results of operations.

A change in accounting policies can have a significant effect on our reported results and may even affect our reporting of transactions completed before the change is effective. New pronouncements and varying interpretations of existing pronouncements have occurred with frequency and may occur in the future. Changes to existing rules, or changes to the interpretations of existing rules, could lead to changes in our accounting practices, and such changes could adversely affect our reported financial results or the way we conduct our business.

The Financial Accounting Standards Board (FASB) issued a new accounting standard for revenue recognition in May 2014 Accounting Standards Update No. (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)* that supersedes nearly all existing U.S. GAAP revenue recognition guidance. Although we are currently in the process of evaluating the impact of ASU 2014-09 on our consolidated financial statements, it is likely to change the way we account for certain of our sales transactions in fiscal 2018, the first year that such new rules will be effective for us. Adoption of the standard could have a significant impact on our financial statements and may retroactively affect the accounting treatment of transactions completed before adoption.

Item 1B. UNRESOLVED STAFF COMMENTS

None.

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Location	Principal Use	Square Feet
<u>Owned Facilities</u>		
Acton, Massachusetts	Corporate Headquarters, Engineering, Customer Services, Manufacturing, Marketing and Human Resources	120,000
Greenville, New Hampshire	Subleased	24,000
<u>Leased Facilities</u>		
Eindhoven, The Netherlands	Engineering, Sales and Customer Services	20,553
Milpitas, California	Engineering	20,155
Manila, Philippines	Engineering and Customer Services	14,175
Portland, Oregon	Engineering	9,557

In addition, we lease offices in Ft. Washington, Pennsylvania, Ireland, India and Turkey. We believe that existing facilities are adequate to meet our foreseeable requirements.

Item 3. LEGAL PROCEEDINGS

We enter into agreements in the ordinary course of business with customers, resellers, distributors, integrators and suppliers. Most of these agreements require us to defend and/or indemnify the other party against intellectual property infringement claims brought by a third party with respect to our products. From time to time, we also indemnify customers and business partners for damages, losses and liabilities they may suffer or incur relating to personal injury, personal property damage, product liability, and environmental claims relating to the use of our products and services or resulting from the acts or omissions of us, our employees, authorized agents or subcontractors. From time to time, we have received requests from customers for indemnification of patent litigation claims. Management cannot reasonably estimate any potential losses, but these claims could result in material liability for us.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

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Our common stock is traded on NASDAQ under the symbol SEAC .

The following table sets forth the quarterly high and low closing sales prices per share reported on NASDAQ for our last two fiscal years ended January 31, 2015 and 2014.

	Fiscal Year 2015		Fiscal Year 2014	
	High	Low	High	Low
Three Month Period Ended:				
First Quarter	\$ 12.27	\$ 9.26	\$ 12.08	\$ 10.50
Second Quarter	9.71	7.49	12.58	10.51
Third Quarter	7.97	6.48	15.12	9.97
Fourth Quarter	7.45	5.43	14.86	11.11

On April 2, 2015, there were 149 holders of record.

We have never declared or paid any cash dividends on our common stock, since inception, and do not expect to pay cash dividends on our common stock in the foreseeable future. We currently intend to retain all of our future earnings for use in operations and to finance the expansion of our business.

Issuer Purchases of Equity Securities***Stock Repurchase Plans***

On September 4, 2013, our Board of Directors authorized the repurchase of up to \$25.0 million of our common stock through a share repurchase program which would have terminated on January 31, 2015. On May 31, 2014, this program was amended to increase the authorized repurchase amount to \$40.0 million and extend the termination date to April 30, 2015. Under the program, we are authorized to repurchase shares through Rule 10b5-1 plans, open market purchases, privately negotiated transactions, block purchases or otherwise in accordance with applicable federal securities laws, including Rule 10b-18 of the Securities Exchange Act of 1934. This share repurchase program does not obligate us to acquire any specific number of shares and may be suspended or discontinued at any time. All repurchases are expected to be funded from our current cash and investment balances. The timing and amount of shares to be repurchased will be based on market conditions and other factors, including price, corporate and regulatory requirements, and alternative investment opportunities. Any shares repurchased by us under the share repurchase program will reduce the number of shares outstanding. Pursuant to the share repurchase program, we executed a Rule 10b5-1 plan in June 2014 to repurchase shares. We used \$5.5 million of cash in connection with the repurchase of 591,520 shares of our common stock (an average price of \$9.31 per share) in fiscal 2015. As of January 31, 2015, \$34.5 million remained available for repurchase under the existing share repurchase authorization.

Stock Performance Graph

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The following graph compares the change in the cumulative total stockholder return on SeaChange's common stock during the period from the close of trading on January 31, 2010 through January 31, 2015, with the cumulative total return on the Center for Research in Securities Prices (CRSP) Index for NASDAQ (U.S. Companies) and a SIC Code Index based on SeaChange's SIC Code. The comparison assumes \$100 was invested on January 29, 2010 in SeaChange's common stock at the \$6.47 closing price on January 29, 2010 and in each of the foregoing indices and assumes reinvestment of dividends, if any.

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The following graph is not soliciting material, is not deemed filed with the SEC and is not to be incorporated by reference in any filing of SeaChange under the Securities Act or the Exchange Act, whether made before or after the date hereof and irrespective of any general incorporation language in any such filing. The stock price performance shown on the following graph is not necessarily indicative of future price performance. Information used on the graph was obtained from a third-party provider, a source believed to be reliable, but SeaChange is not responsible for any errors or omissions in such information.

Notes:

- (1) The lines represent monthly index levels derived from compounded daily returns that include all dividends.
- (2) If the monthly interval, based on the fiscal year end, is not a trading day, the preceding trading day is used.
- (3) The index level for all series was set to 100 on January 31, 2010.

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Our selected financial data below should be read in conjunction with our audited, consolidated financial statements and related notes contained in Part II, Item 8., *Financial Statements and Supplementary Data*, of this Form 10-K. For all periods presented, this selected financial data have been adjusted to reflect the businesses divested as discontinued operations.

CONSOLIDATED STATEMENTS OF OPERATIONS DATA

	For the Fiscal Years Ended January 31,				
	2015	2014	2013	2012	2011
	(Amounts in thousands, except per share data)				
Product revenue	\$ 31,507	\$ 54,749	\$ 64,274	\$ 73,157	\$ 82,155
Service revenue	83,928	91,570	92,914	91,635	91,500
Total revenues	115,435	146,319	157,188	164,792	173,655
Total operating costs and expenses	(141,888)	(147,948)	(162,534)	(166,462)	(171,669)
Other (expense) income, net	(2,161)	(224)	(86)	6	(880)
(Loss) gain on sale of investment in affiliates		(363)	885		27,071
(Loss) income before income taxes and equity income in earnings of affiliates	(28,614)	(2,216)	(4,547)	(1,664)	28,177
Income tax (benefit) provision	(1,106)	55	(1,555)	1,881	(2,227)
Equity income in earnings of affiliates, net of tax	19	44	193	142	167
Net (loss) income from continuing operations	(27,489)	(2,227)	(2,799)	(3,403)	30,571
Loss on sale of discontinued operations			(14,073)		
Income (loss) from discontinued operations, net	5	(803)	(2,293)	(611)	(1,103)
Net (loss) income	\$ (27,484)	\$ (3,030)	\$ (19,165)	\$ (4,014)	\$ 29,468
(Loss) earnings per share:					
Basic	\$ (0.84)	\$ (0.09)	\$ (0.59)	\$ (0.13)	\$ 0.94
Diluted	\$ (0.84)	\$ (0.09)	\$ (0.59)	\$ (0.13)	\$ 0.92
(Loss) earnings per share from continuing operations:					
Basic	\$ (0.84)	\$ (0.07)	\$ (0.09)	\$ (0.11)	\$ 0.98
Diluted	\$ (0.84)	\$ (0.07)	\$ (0.09)	\$ (0.11)	\$ 0.96
Income (loss) per share from discontinued operations:					
Basic	\$ 0.00	\$ (0.02)	\$ (0.50)	\$ (0.02)	\$ (0.04)
Diluted	\$ 0.00	\$ (0.02)	\$ (0.50)	\$ (0.02)	\$ (0.04)

CONSOLIDATED BALANCE SHEET DATA

	As of January 31,				
	2015	2014	2013	2012	2011
	(Amounts in thousands)				
Working capital	\$ 101,014	\$ 125,875	\$ 116,922	\$ 103,290	\$ 92,846
Total assets	212,351	254,113	264,676	298,852	305,191
Deferred revenue	19,088	25,628	30,603	35,735	39,783
Long-term liabilities	6,266	6,670	7,815	21,685	27,275
Total liabilities	41,300	49,672	62,475	87,914	96,049
Total stockholders' equity	171,051	204,441	202,201	210,938	209,142

Table of Contents**Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (MD&A)**

The following discussion should be read in conjunction with our consolidated financial statements and accompanying notes included in this Form 10-K. When reviewing the discussion, you should keep in mind the substantial risks and uncertainties that characterize our business. In particular, we encourage you to review the risk and uncertainties described under Item 1A., *Risk Factors*, of this Form 10-K. These risks and uncertainties could cause actual results to differ materially from those forecasted in forward-looking statements or implied by past results and trends. Forward-looking statements are statements that attempt to project or anticipate future developments in our business; we encourage you to review the discussion of forward-looking statements under *Cautionary Statement for Purposes of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995*, at the beginning of this report. These statements, like all statements in this report, speak only as of the date of this report (unless another date is indicated), and we undertake no obligation to update or revise the statements in light of future developments. Unless otherwise specified, any reference to a year is to a fiscal year ended January 31st.

Business Overview

We are an industry leader in the delivery of multiscreen video headquartered in Acton, Massachusetts. Our products and services facilitate the aggregation, licensing, management and distribution of video and advertising content for cable television system operators, telecommunications and media companies (television networks, movie studios and broadcasters). We currently operate under one reporting segment.

In fiscal 2016, we expect to continue addressing what we see as the continuing rise of over-the-top (OTT) services by such companies as Netflix, Hulu and Amazon and by media companies such as HBO, CBS and BBC. This rise of OTT video services in the United States has increased the demand for multiscreen capabilities on a range of consumer devices operating on cloud-based platforms. We have been increasing our strategic investments in research and development related to our cloud-based offerings, as well as in sales and marketing as we work to increase our go-to-market efforts in this area.

We plan to invest in Rave, our cloud-based SaaS offering, which permits service providers and media companies to offer features and functions through a service hosted and managed by SeaChange, reducing cost and increasing speed and ease of use for end-users. We believe that delivering innovative solutions to both our existing customer base and to content owners that are looking to provide OTT services, we can meet their growing needs and help them get to market faster that will help them drive new revenue growth. Recognizing the importance of OTT, we have architected our cloud solutions and products to make integrating with existing networks simple and a core competency of our platform. We have optimized our software solutions to serve a wide range of consumer devices.

We expect that revenue from our next generation products will continue to grow during fiscal 2016. This is driven by increasing market acceptance of both Adrenalin and Nucleus. We believe that we have the opportunity for continued revenue growth by expanding our selling efforts in new geographic areas such as Asia Pacific and Latin America. We also believe that our existing service operator customers will need to upgrade to the next generation product to enable the capacity to increase average revenue per subscriber, reduce operating and capital expenses, and lower customer churn. During fiscal 2015, we continued to generate new design wins driven by growth of Adrenalin and market introduction of our Nucleus product. We also achieved our first win with a media company for an OTT solution that will be deployed in fiscal 2016 and several service providers have entered into trials of our Rave product.

On February 2, 2015, we acquired Timeline Labs, a California-based software-as-a-service (SaaS) company that enables local broadcasters, national news organizations and other media companies and brands to analyze

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social media messages in real-time, find and broadcast social trends, and measure viewing audience engagements across television, mobile and personal computers.

We continue to experience fluctuations in our revenues from period to period due to the following factors:

Budgetary approvals by our customers for capital purchases;

The ability of our customers to process the purchase order within their organization in a timely manner;

The time required to deliver and install the product and for the customer to accept the product and services;

Declines in sales of legacy products; and

Uncertainty caused by potential consolidation in the industry.

In addition, many customers may delay or reduce capital expenditures. This, together with other factors, could result in the reductions in sales of our products, longer sales cycles, difficulties in collection of accounts receivable, a longer period of time before we may recognize revenue attributable to a sale, excess and obsolete inventory, gross margin deterioration, slower adoption of new technologies, the transition to SaaS, and increased price competition.

In January 2015, we initiated a global restructuring plan to streamline our activities, primarily from an employee headcount reduction of 10%, now that our next generation software products have been brought to market and are being deployed around the globe. The reduction in workforce was implemented immediately in the United States and, to comply with non-U.S. legal requirements, will be implemented on an international basis over the next several quarters. Once fully implemented, we expect this initiative to yield approximately \$11 million in annualized cost savings.

Results of Operations

The following discussion summarizes the key factors our management believes are necessary for an understanding of our consolidated financial statements.

Revenues

The components of our total revenues are described in the following table:

	For the Fiscal Years Ended January 31,			FY15 vs. FY14		FY14 vs. FY13	
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
Software Revenues:	(Amounts in thousands, except for percentage data)						

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Products	\$ 31,507	\$ 54,749	\$ 64,274	\$ (23,242)	(42.5%)	\$ (9,525)	(14.8%)
Services	83,928	91,570	92,914	(7,642)	(8.3%)	(1,344)	(1.4%)
Total revenues	115,435	146,319	157,188	(30,884)	(21.1%)	(10,869)	(6.9%)
Cost of product revenues	9,915	11,795	19,826	(1,880)	(15.9%)	(8,031)	(40.5%)
Cost of service revenues	48,413	55,325	52,319	(6,912)	(12.5%)	3,006	5.7%
Inventory write-down			1,752		N/A	(1,752)	(100.0%)
Total cost of revenues	58,328	67,120	73,897	(8,792)	(13.1%)	(6,777)	(9.2%)
Gross profit	\$ 57,107	\$ 79,199	\$ 83,291	\$ (22,092)	(27.9%)	\$ (4,092)	(4.9%)
Gross product profit margin	68.5%	78.5%	69.2%		(10.0%)		9.3%
Gross service profit margin	42.3%	39.6%	43.7%		2.7%		(4.1%)
Gross profit margin	49.5%	54.1%	53.0%		(4.6%)		1.1%

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Fiscal 2015 As Compared to Fiscal 2014

Product Revenue. Product revenue in fiscal 2015 decreased \$23.2 million, or 43%, as compared to fiscal 2014 due primarily to:

a \$14.0 million decrease in our legacy middleware product line;

a \$6.6 million decrease in revenue from our multiscreen video platform primarily in Europe and South America; and

a \$2.6 million decrease primarily related to lower revenue from our legacy VOD backoffice products. The \$16.6 million decline in revenue from legacy products is consistent with our expectations for fiscal 2015. We expect revenues from our legacy products to continue to decrease in fiscal 2016. The decline in revenue from legacy products will be offset by an increase in our next generation product revenue.

Service Revenue. Service revenue decreased \$7.6 million, or 8%, for fiscal 2015, when compared to fiscal 2014, primarily due to lower video gateway service revenue and lower installation revenues due to lower product revenues.

For fiscal 2015, two customers each accounted for more than 10%, and collectively accounted for 32% of our total revenues. For fiscal 2014, three customers each accounted for more than 10%, and collectively accounted for 49% of our total revenues. We believe that a significant amount of our revenues will continue to be derived from a limited number of customers.

International revenues accounted for approximately 48%, or \$55.6 million, and 54%, or \$79.4 million, of total revenues in fiscal 2015 and 2014, respectively. The strengthening of the U.S. dollar against the Euro adversely impacted revenue by approximately \$1.9 million in fiscal 2015. Since January 31, 2015, the U.S. dollar has continued to strengthen against the Euro, therefore, we expect that revenue will continue to be impacted next fiscal year as international revenues remain a significant portion of our business.

Gross Profit and Margin. Cost of product revenues consists primarily of the cost of resold third-party products and services, purchased components and subassemblies, labor and overhead relating to the assembly and testing of complete systems and costs related to customized software development contracts.

Our gross profit margin decreased approximately five percentage points for fiscal 2015, as compared to fiscal 2014. This decrease in gross profit margin was primarily due to a 10 percentage point decrease in gross product profit margin to 69% for fiscal 2015, primarily due to lower legacy middleware revenue, which carried high margins, offset by a three percentage point increase in gross service profit margin to 42% for fiscal 2015, compared to fiscal 2014, primarily due to a mix of lower video gateway service revenue, as mentioned above, which carry lower margins due to the customer-specific requirements.

Fiscal 2014 As Compared to Fiscal 2013

Product Revenue. Product revenue decreased \$9.5 million, or 15%, for fiscal 2014 as compared to fiscal 2013 due primarily to:

a \$13.3 million decrease in our revenues from legacy products, primarily in our advertising sales to our North American customers and VOD server product lines primarily to South American customers; and

\$3.1 million in lower video gateway license revenues due to a significant licensing transaction with a customer in Europe during fiscal 2013; offset by

a \$3.0 million increase in revenues from our legacy middleware product line; and

a \$3.9 million increase in revenues from our multiscreen video platform sales to large North American customers.

Service Revenue. Service revenue for fiscal 2014 decreased \$1.3 million as compared to fiscal 2013. This is primarily related to a \$2.5 million decrease in our legacy middleware service revenues as a result of a fiscal 2013 amendment with a European customer which resulted in a higher portion of revenue to be recognized as product revenue in fiscal 2014. This decrease was partially offset by higher customization service revenues primarily for our next generation multiscreen platform products.

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Gross Profit and Margin. Our gross profit margin increased one percentage point for fiscal year ended January 31, 2014, as compared to fiscal 2013, net of the inventory write-down recorded during the second quarter of fiscal 2013.

This is primarily due to the following:

A four percentage point decrease in gross service profit margin to 40% for fiscal 2014, compared to fiscal 2013, primarily due to the mix of higher customized development revenues which typically carry lower margins due to higher costs of research and development personnel; offset by

A nine percentage point increase in gross product profit margin to 79% for fiscal 2014, primarily due to a mix of higher software licensing revenues and lower VOD server revenues, which typically carry lower margins.

Operating Expenses***Research and Development***

The following table provides information regarding the change in research and development expenses during the periods presented:

	For the Fiscal Years Ended January 31,		FY15 vs. FY14		FY14 vs. FY13		
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
	(Amounts in thousands, except for percentage data)						
Research and development expenses	\$ 42,169	\$ 39,657	\$ 38,667	\$ 2,512	6.3%	\$ 990	2.6%
% of total revenue	36.5%	27.1%	24.6%				

Fiscal 2015 As Compared to Fiscal 2014

Research and development expenses consist primarily of employee costs, which include salaries, benefits and related payroll taxes, depreciation of development and test equipment and an allocation of related facility expenses. Research and development costs increased \$2.5 million in fiscal 2015 as compared to fiscal 2014. The increase is related to our investment in our video gateway software product, Nucleus, and our cloud-based platform, Rave.

Fiscal 2014 As Compared to Fiscal 2013

During fiscal 2014, our total research and development expenses increased \$1.0 million, or 3%, as compared to fiscal 2013, due primarily to an increase in outside contract labor costs as we continue to focus our investment in research and development related to our next generation product offerings.

Selling and Marketing

The following table provides information regarding the change in selling and marketing expenses during the periods presented:

	For the Fiscal Years Ended January 31,			FY15 vs. FY14		FY14 vs. FY13	
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
	(Amounts in thousands, except for percentage data)						
Selling and marketing expenses	\$ 13,920	\$ 15,018	\$ 15,398	\$ (1,098)	(7.3%)	\$ (380)	(2.5%)
% of total revenue	12.1%	10.3%	9.8%				

Table of Contents*Fiscal 2015 As Compared to Fiscal 2014*

Selling and marketing expenses consist primarily of payroll costs, which include salaries and related payroll taxes, benefits and commissions, travel expenses and certain promotional expenses. Selling and marketing expenses decreased \$1.1 million, or 7%, in fiscal 2015 when compared to fiscal 2014. This reduction was primarily related to lower employee related costs due to a reduction in headcount, and to lower commissions resulting from lower revenues.

Fiscal 2014 As Compared to Fiscal 2013

Selling and marketing expenses decreased \$0.4 million, or 3%, in fiscal 2014, when compared to fiscal 2013 due to lower commission expense resulting from lower revenues and a reduction in headcount compared to the prior fiscal year.

General and Administrative

The following table provides information regarding the change in general and administrative expenses during the periods presented:

	For the Fiscal Years Ended January 31,			FY15 vs. FY14		FY14 vs. FY13	
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
	(Amounts in thousands, except for percentage data)						
General and administrative expenses	\$ 16,014	\$ 17,618	\$ 17,674	\$ (1,604)	(9.1%)	\$ (56)	(0.3%)
% of total revenue	13.9%	12.0%	11.2%				

Fiscal 2015 As Compared to Fiscal 2014

General and administrative expenses consist primarily of employee costs, which include salaries and related payroll taxes and benefit-related costs, legal and accounting services and an allocation of related facilities expenses. General and administrative expenses decreased \$1.6 million, or 9%, in fiscal 2015, as compared to fiscal 2014, primarily due to a decrease in employee costs from a lower headcount year over year.

Fiscal 2014 As Compared to Fiscal 2013

General and administrative expenses remained relatively stable during fiscal 2014, as compared to fiscal 2013.

Amortization of Intangible Assets

The following table provides information regarding the change in amortization of intangible assets during the periods presented:

	For the Fiscal Years Ended January 31,			FY15 vs. FY14		FY14 vs. FY13	
	2015	2014	2013	% Change	\$ Change	% Change	\$ Change

Table of Contents***Stock-based Compensation Expense***

The following table provides information regarding the change in stock-based compensation expense during the periods presented:

	For the Fiscal Years Ended January 31, FY15 vs. FY14				FY14 vs. FY13		
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
	(Amounts in thousands, except for percentage data)						
Stock-based compensation expense	\$ 3,220	\$ 2,959	\$ 5,929	\$ 261	8.8%	\$ (2,970)	(50.1%)
% of total revenue	2.8%	2.0%	3.8%				

Fiscal 2015 As Compared to Fiscal 2014

Stock-based compensation expense is primarily due to the issuance of stock grants to our employees, executives and members of our Board of Directors. Stock-based compensation expense increased \$0.3 million during fiscal 2015 as compared to fiscal 2014 related to additional stock compensation expense recorded as a result of our separation agreement with the former Chief Executive Officer (CEO) and the hiring of our new CEO.

Fiscal 2014 As Compared to Fiscal 2013

Stock-based compensation expense decreased \$3.0 million during fiscal 2014, as compared to fiscal 2013 primarily due to higher stock-based compensation related to the performance-based stock compensation granted to our now former CEO, who was appointed to his permanent position on May 1, 2012.

Earn-outs and Change in Fair Value of Earn-outs

The following table provides information regarding the change in earn-outs and change in fair value of earn-out expenses during the periods presented:

	For the Fiscal Years Ended January 31, FY15 vs. FY14				FY14 vs. FY13		
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
	(Amounts in thousands, except for percentage data)						
Earn-outs and change in fair value of earn-outs	\$	\$ (60)	\$ 2,435	\$ 60	(100.0%)	\$ (2,495)	>(100%)
% of total revenue	0.0%	0.0%	1.5%				

During fiscal 2013 we incurred \$2.4 million of earn-out expenses for payments made in connection with certain of our acquisitions in accordance with the respective earn-out criteria being met.

Professional Fees Other

The following table provides information regarding the change in professional fees expenses associated with acquisitions, divestitures, litigation and strategic alternatives during the periods presented:

For the Fiscal Years Ended January 31, FY15 vs. FY14 FY14 vs. FY13
2015 2014 2013 \$ Change % Change \$ Change % Change
(Amounts in thousands, except for percentage data)

Professional fees other	\$ 671	\$ 1,614	\$ 1,619	\$ (943)	(58.4%)	\$ (5)	(0.3%)
% of total revenue	0.6%	1.1%	1.0%				

Professional fees in fiscal 2015 decreased \$0.9 million when compared to fiscal 2014 primarily due to a decrease in costs related to patent litigation and remained relatively stable in fiscal 2014 when compared to fiscal 2013.

Table of Contents***Severance and Other Restructuring Expenses***

The following table provides information regarding the change in severance and other restructuring expenses during the periods presented:

	For the Fiscal Years Ended January 31,			FY15 vs. FY14		FY14 vs. FY13	
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
	(Amounts in thousands, except for percentage data)						
Severance and other restructuring expenses	\$ 3,623	\$ 911	\$ 3,106	\$ 2,712	>100%	\$ (2,195)	(70.7%)
% of total revenue	3.1%	0.6%	2.0%				
<i>Fiscal 2015 As Compared to Fiscal 2014</i>							

Severance and other restructuring costs increased \$2.7 million in fiscal 2015, as compared to fiscal 2014, primarily due to the separation agreement with our former CEO and a reduction in workforce during fiscal 2015.

Fiscal 2014 As Compared to Fiscal 2013

For fiscal 2014, we incurred severance charges of \$0.9 million related to a reduction in force during the fiscal year, compared to \$1.9 million in severance charges during fiscal 2013. In addition, fiscal 2013 included a \$0.8 million leasehold improvement charge for the reduction of space and certain fixed assets in our leased facility in the Philippines, and \$0.4 million of other restructuring charges.

Other (Expense) Income, Net

The table below provides detail regarding our other (expense) income, net:

	For the Fiscal Years Ended January 31,			FY15 vs. FY14		FY14 vs. FY13	
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
	(Amounts in thousands, except for percentage data)						
(Loss) gain on sale of investment in affiliates	\$	\$ (363)	\$ 885	\$ 363	(100.0%)	\$ (1,248)	>(100%)
Interest income, net	211	251	26	(40)	(15.9%)	225	>100%
Foreign exchange loss	(2,348)	(367)	(23)	(1,981)	>100%	(344)	>(100%)
Miscellaneous expense	(24)	(108)	(89)	84	(77.8%)	(19)	21.3%
	\$ (2,161)	\$ (587)	\$ 799	\$ (1,574)		\$ (1,386)	

Foreign exchange loss

During fiscal 2015, loss on foreign exchange increased \$2.0 million due to the increased strength of the U.S. Dollar compared to other foreign currencies, primarily the Euro.

(Loss) gain on sale of investment in affiliates

During fiscal 2014, we recorded a loss of \$0.4 million on the sale of an investment in affiliates during the second quarter. This is compared to a \$0.9 million gain on sale of an equity investment recorded in fiscal 2013.

Income Tax (Benefit) Provision

	For the Fiscal Years Ended January 31,			FY15 vs. FY14		FY14 vs. FY13	
	2015	2014	2013	\$ Change	% Change	\$ Change	% Change
	(Amounts in thousands, except for percentage data)						
Income tax (benefit) provision	\$ (1,106)	\$ 55	\$ (1,555)	\$ (1,161)	>(100%)	\$ 1,610	>100%
% of total revenue	(1.0%)	0.0%	(1.0%)				

Table of Contents*Fiscal 2015 As Compared to Fiscal 2014*

We recorded an income tax benefit from continuing operations of \$1.1 million in fiscal 2015. Our effective tax rate is lower than the U.S. federal statutory rate as we did not record tax benefits on our year-to-date losses in certain jurisdictions, including the United States, where we continue to maintain a full valuation allowance against deferred tax assets. Additionally, the rate is impacted by the geographic jurisdiction in which the worldwide income or loss will be incurred, resulting in the difference between the federal statutory rate of 35% and the forecasted effective tax rate. The tax benefit includes the reversal of tax reserves for uncertain tax positions due to the expiration of the statute of limitations. The statute of limitations varies in each jurisdiction we operate in. In any given year, a jurisdiction's statute of limitations may lapse without examination and any tax reserves for uncertain tax positions recorded in a corresponding year will result in the reduction of the liability for unrecognized tax benefits for that year.

Our effective tax rate may fluctuate on a quarterly basis as a result of changes in the valuation of our deferred tax assets, changes in actual results versus our estimates, or changes in tax laws, regulations, accounting principles, or interpretations thereof. We regularly review our tax positions in each significant taxing jurisdiction in the process of evaluating our unrecognized tax benefits. We make adjustments to our unrecognized tax benefits when: i) facts and circumstance regarding a tax position change, causing a change in management's judgment regarding that tax position; ii) a tax position is effectively settled with a tax authority; and/or iii) the statute of limitations expires regarding a tax position.

We continue to maintain a valuation allowance against deferred tax assets where realization is not certain. We periodically evaluate the likelihood of the realization of deferred tax assets and reduce the carrying amount of these deferred tax assets by a valuation allowance to the extent we believe a portion will not be realized.

Fiscal 2014 As Compared to Fiscal 2013

For fiscal 2014, we recorded an income tax provision of \$0.1 million primarily due to state income taxes.

Non-GAAP Measures

We define non-GAAP (loss) income from operations as U.S. GAAP operating (loss) income plus stock-based compensation expenses, amortization of intangible assets, earn-outs and change in fair value of earn-outs, professional fees associated with acquisitions, divestitures, litigation and strategic alternatives and severance and other restructuring costs. We define adjusted EBITDA as U.S. GAAP operating (loss) income before depreciation expense, amortization of intangible assets, stock-based compensation expense, earn-outs and change in fair value of earn-outs, professional fees associated with acquisitions, divestitures, litigation and strategic alternatives, and severance and other restructuring costs. We discuss non-GAAP (loss) income from operations in our quarterly earnings releases and certain other communications as we believe non-GAAP operating (loss) income from operations and adjusted EBITDA are both important measures that are not calculated according to U.S. GAAP. We use non-GAAP (loss) income from operations and adjusted EBITDA in internal forecasts and models when establishing internal operating budgets, supplementing the financial results and forecasts reported to our Board of Directors, determining a component of bonus compensation for executive officers and other key employees based on operating performance and evaluating short-term and long-term operating trends in our operations. We believe that non-GAAP (loss) income from operations and adjusted EBITDA financial measures assist in providing an enhanced understanding of our underlying operational measures to manage the business, to evaluate performance compared to prior periods and the marketplace, and to establish operational goals. We believe that these non-GAAP financial adjustments are useful to investors because they allow investors to evaluate the effectiveness of the methodology and information used by management in our financial and operational decision-making.

Non-GAAP (loss) income from operations and adjusted EBITDA are non-GAAP financial measures and should not be considered in isolation or as a substitute for financial information provided in accordance with U.S. GAAP. These non-GAAP financial measures may not be computed in the same manner as similarly titled measures used by other companies. We expect to continue to incur expenses similar to the financial adjustments described above in arriving at non-GAAP (loss) income from operations and adjusted EBITDA, and investors should not infer from our presentation of this non-GAAP financial measure that these costs are unusual, infrequent or non-recurring.

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The following table includes the reconciliations of our U.S. GAAP (loss) income from operations, the most directly comparable U.S. GAAP financial measure, to our non-GAAP (loss) income from operations and the reconciliation of our U.S. GAAP (loss) income from operations to our adjusted EBITDA for fiscal 2015, 2014 and 2013 (amounts in thousands, except per share and percentage data):

	For the Fiscal Year Ended January 31, 2015			For the Fiscal Year Ended January 31, 2014			For the Fiscal Year Ended January 31, 2013		
	GAAP As Reported	Adjustments	Non-GAAP	GAAP As Reported	Adjustments	Non-GAAP	GAAP As Reported	Adjustments	Non-GAAP
Revenues:									
Products	\$ 31,507	\$	\$ 31,507	\$ 54,749	\$	\$ 54,749	\$ 64,274	\$	\$ 64,274
Services	83,928		83,928	91,570		91,570	92,914		92,914
Total Revenues	115,435		115,435	146,319		146,319	157,188		157,188
Cost of Revenues:									
Products	8,845		8,845	10,526		10,526	17,397		17,397
Services	48,272		48,272	55,075		55,075	52,162		52,162
Amortization of intangible assets	1,070	(1,070)		1,269	(1,269)		2,429	(2,429)	
Stock-based compensation	141	(141)		250	(250)		157	(157)	
Inventory write-down							1,752	(1,752)	
Total cost of Revenues	58,328	(1,211)	57,117	67,120	(1,519)	65,601	73,897	(4,338)	69,559
Gross profit	57,107	1,211	58,318	79,199	1,519	80,718	83,291	4,338	87,629
Gross profit percentage	49.5%	1.0%	50.5%	54.1%	1.0%	55.2%	53.0%	2.8%	55.7%
Operating Expenses:									
Research and development	42,169		42,169	39,657		39,657	38,667		38,667
Selling and marketing	13,920		13,920	15,018		15,018	15,398		15,398
General and administrative	16,014		16,014	17,618		17,618	17,674		17,674
Amortization of intangible assets	4,084	(4,084)		3,361	(3,361)		3,966	(3,966)	

Stock-based compensation expense	3,079	(3,079)		2,709	(2,709)		5,772	(5,772)	
Turn-outs and change in fair value of turn-outs				(60)	60		2,435	(2,435)	
Professional fees other	671	(671)		1,614	(1,614)		1,619	(1,619)	
Overance and other structuring costs	3,623	(3,623)		911	(911)		3,106	(3,106)	
Total operating expenses	83,560	(11,457)	72,103	80,828	(8,535)	72,293	88,637	(16,898)	71,739
(Loss) income from operations	\$ (26,453)	\$ 12,668	\$ (13,785)	\$ (1,629)	\$ 10,054	\$ 8,425	\$ (5,346)	\$ 21,236	\$ 15,890
(Loss) income from operations percentage weighted average common shares outstanding:									
Basic	(22.9%)	11.0%	(11.9%)	(1.1%)	6.9%	5.8%	(3.4%)	13.5%	10.1%
Adjusted									
Basic	32,772	32,772	32,772	32,718	32,718	32,718	32,494	32,093	32,494
Adjusted	32,772	33,004	32,772	32,718	33,572	33,572	32,494	32,989	32,989
Non-GAAP operating (loss) income per share:									
Basic	\$ (0.81)	\$ 0.39	\$ (0.42)	\$ (0.05)	\$ 0.31	\$ 0.26	\$ (0.16)	\$ 0.65	\$ 0.49
Adjusted	\$ (0.81)	\$ 0.39	\$ (0.42)	\$ (0.05)	\$ 0.30	\$ 0.25	\$ (0.16)	\$ 0.64	\$ 0.48
Adjusted EBITDA:									
Loss from operations			\$ (26,453)			\$ (1,629)			\$ (5,346)
Depreciation expense			3,683			4,389			4,671
			5,154			4,630			6,395

Amortization of intangible assets			
Stock-based compensation expense	3,220	2,959	5,929
Spin-outs and changes in fair value		(60)	2,435
Professional fees other	671	1,614	1,619
Inventory write-down			1,752
Lease and other restructuring	3,623	911	3,106
Adjusted EBITDA	\$ (10,102)	\$ 12,814	\$ 20,561
Adjusted EBITDA %	(8.8%)	8.8%	13.1%

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In managing and reviewing our business performance, we exclude a number of items required by U.S. GAAP. Management believes that excluding these items is useful in understanding the trends and managing our operations. We provide these supplemental non-GAAP measures in order to assist the investment community to see SeaChange through the eyes of management, and therefore enhance the understanding of our operating performance. Non-GAAP financial measures should be viewed in addition to, not as an alternative to, our reported results prepared in accordance with U.S. GAAP. Our non-GAAP financial measures reflect adjustments based on the following items:

Amortization of Intangible Assets. We incur amortization expense of intangible assets related to various acquisitions that have been made in recent years. These intangible assets are valued at the time of acquisition, are then amortized over a period of several years after the acquisition and generally cannot be changed or influenced by management after the acquisition. We believe that exclusion of these expenses allows comparisons of operating results that are consistent over time for the Company's newly-acquired and long-held businesses.

Stock-based Compensation Expense. We incur expenses related to stock-based compensation included in our U.S. GAAP presentation of cost of revenues, selling and marketing expense, general and administrative expense and research and development expense. Although stock-based compensation is an expense we incur and is viewed as a form of compensation, the expense varies in amount from period to period, and is affected by market forces that are difficult to predict and are not within the control of management, such as the market price and volatility of our shares, risk-free interest rates and the expected term and forfeiture rates of the awards.

Inventory Write-down. We incur inventory write-downs of our legacy product lines as we end the life of certain product lines to focus on selling the new products being developed.

Earn-outs and Change in Fair Value of Earn-outs. Earn-outs and the change in the fair value of the earn-outs are considered by management to be non-recurring expenses to the former shareholders of the businesses we acquire. We also incur expense due to changes in fair value related to contingent consideration that we believe would otherwise impair comparability among periods.

Professional Fees Other. We have excluded the effect of legal and other professional costs associated with our acquisitions, divestitures, litigation and strategic alternatives because the amounts are considered to be significant non-operating expenses.

Severance and Other Restructuring. We incur charges due to the restructuring of our business, including severance charges and facility reductions resulting from our restructuring and streamlining efforts and any changes due to revised estimates, which we generally would not have otherwise incurred in the periods presented as part of our continuing operations.

Depreciation Expense. We incur depreciation expense related to capital assets purchased to support the ongoing operations of the business. These assets are recorded at cost and are depreciated using the straight-line method over the useful life of the asset. Purchases of such assets may vary significantly from period to period and without any correlation to underlying operating performance. Management believes that exclusion of depreciation expense allows comparisons of operating results that are consistent across past, present and future periods.

Table of Contents**Liquidity and Capital Resources**

The following table includes key line items of our consolidated statements of cash flows:

	For the Fiscal Years Ended January 31,			FY15 vs FY14	FY14 vs FY13
	2015	2014	2013	\$ Change	\$ Change
	(Amounts in thousands)				
Total cash (used in) provided by operating activities	\$ (13,339)	\$ 7,364	\$ 17,357	\$ (20,703)	\$ (9,993)
Total cash (used in) provided by investing activities	(8,156)	520	12,994	(8,676)	(12,474)
Total cash (used in) provided by financing activities	(5,504)	1,058	(4,009)	(6,562)	5,067
Effect of exchange rate changes on cash	1,284	71	(206)	1,213	277
Net (decrease) increase in cash	\$ (25,715)	\$ 9,013	\$ 26,136	\$ (34,728)	\$ (17,123)

Historically, we have financed our operations and capital expenditures primarily with cash on-hand. Cash and cash equivalents, restricted cash and marketable securities decreased from \$128.1 million at January 31, 2014 to \$105.4 million at January 31, 2015.

We believe that existing funds combined with available borrowings under the line of credit and cash provided by future operating activities are adequate to satisfy our working capital, potential acquisitions and capital expenditure requirements and other contractual obligations for the foreseeable future, including at least the next 12 months. However, if our expectations are incorrect, we may need to raise additional funds to fund our operations, to take advantage of unanticipated strategic opportunities or to strengthen our financial position. In the future, we may enter into other arrangements for potential investments in, or acquisitions of, complementary businesses, services or technologies, which could require us to seek additional equity or debt financing. Additional funds may not be available on terms favorable to us or at all.

Operating Activities

Below are key line items affecting cash from operating activities:

	For the Fiscal Years Ended			FY15 vs FY14	FY14 vs FY13
	2015	January 31,	2013	\$ Change	\$ Change
	(Amounts in thousands)				
Net loss from continuing operations	\$ (27,489)	\$ (2,227)	\$ (2,799)	\$ (25,262)	\$ 572
Adjustments to reconcile net loss to cash (used in) provided by operating activities	12,197	12,092	19,459	105	(7,367)

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Net (loss) income including adjustments	(15,292)	9,865	16,660	(25,157)	(6,795)
Decrease in accounts receivables	1,574	169	6,313	1,405	(6,144)
Decrease (increase) in prepaid expenses and other current assets	1,570	6,724	(5,045)	(5,154)	11,769
Increase (decrease) in accrued expenses	1,650	(3,146)	1,430	4,796	(4,576)
Decrease in deferred revenues	(5,699)	(4,877)	(6,283)	(822)	1,406
All other net	2,853	(568)	2,895	3,421	(3,463)
Net cash (used in) provided by operating activities from continuing operations	(13,344)	8,167	15,970	(21,511)	(7,803)
Net cash provided by (used in) operating activities from discontinued operations	5	(803)	1,387	808	(2,190)
	\$ (13,339)	\$ 7,364	\$ 17,357	\$ (20,703)	\$ (9,993)

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For fiscal 2015, we used net cash from continuing operating activities of \$13.3 million. The decrease was primarily due to a net loss of \$27.5 million, a \$12.2 million net increase in noncash items and a \$1.9 million increase from the net change in other current and noncurrent assets and liabilities. Noncash items primarily consist of stock-based compensation, depreciation of property and equipment, amortization of intangible assets and changes in deferred income taxes.

In fiscal year 2014, we generated net cash from continuing operating activities of \$8.2 million. This cash provided by operating activities was primarily the result of our net loss including adjustments, which provided cash of \$9.9 million, a decrease in prepaid expenses and other current assets of \$6.7 million, primarily due to tax refunds in fiscal 2014 and a \$1.1 million increase in accrued expenses. This amount is partially offset by a \$4.2 million decrease in customer deposits, which are included in accrued expenses, due to the fulfillment of customers' orders in fiscal 2014, a \$4.9 million decrease in deferred revenues due to recognition of previously deferred revenue. Other use of cash from continuing operating activities of \$0.6 million is primarily due to a decrease in accounts payable, due to the timing of payment to our vendors.

Investing Activities

Cash flows from investing activities are as follows:

	For the Fiscal Years Ended				
	2015	January 31, 2014	2013	FY15 vs FY14 \$ Change	FY14 vs FY13 \$ Change
	(Amounts in thousands)				
Purchases of property and equipment and capitalized software	\$(1,873)	\$ (2,315)	\$ (3,972)	\$ 442	\$ 1,657
Purchases of marketable securities	(9,193)	(11,479)	(15,642)	2,286	4,163
Proceeds from sale and maturity of marketable securities	7,181	12,237	14,214	(5,056)	(1,977)
Proceeds from sale of equity investment	229	1,128	885	(899)	243
Investment in affiliate	(2,000)			(2,000)	
Acquisition of businesses and payment of contingent consideration, net of cash acquired		(4,009)	(8,175)	4,009	4,166
Advance for Timeline Labs acquisition	(2,500)			(2,500)	
Other		958	452	(958)	506
Net cash used in investing activities from continuing operations	(8,156)	(3,480)	(12,238)	(4,676)	8,758
Net cash provided by investing activities from discontinued operations		4,000	25,232	(4,000)	(21,232)
	\$ (8,156)	\$ 520	\$ 12,994	\$ (8,676)	\$ (12,474)

We used \$8.2 million of cash in investing activities from continuing operations primarily related to the advance for the Timeline Lab acquisition of \$2.5 million and an investment in affiliate of \$2.0 million. Additionally, we had \$2.0

million of net purchases of marketable securities and \$1.9 million of capital asset purchases.

In fiscal 2014, we used \$3.5 million of cash in investing activities from continuing operations primarily related to the purchase of capital assets of \$2.3 million and \$4.0 million of earn-out payments made in connection with certain of our acquisitions. These cash outlays were offset by \$1.1 million of proceeds from the sale of our equity investments during fiscal 2014, the release of \$0.9 million in restricted cash as we satisfied the commitment secured by performance bonds and \$0.8 million of net proceeds related to the sale of marketable securities. Cash provided by investing activities from discontinued operations included the receipt of \$4.0 million in fiscal 2014 that was previously held in escrow and that was related to the sale of our media services business in fiscal 2013.

Table of Contents***Financing Activities***

Cash flows from financing activities are as follows:

	For the Fiscal Years Ended			FY15 vs	FY14 vs
	2015	January 31, 2014	2013	FY14	FY13
				\$ Change	\$ Change
	(Amounts in thousands)				
Repurchases of our common stock	\$ (5,504)	\$	\$ (6,200)	\$ (5,504)	\$ 6,200
Proceeds from issuance of common stock relating to stock option exercises		1,058	2,191	(1,058)	(1,133)
	\$ (5,504)	\$ 1,058	\$ (4,009)	\$ (6,562)	\$ 5,067

We used \$5.5 million in cash from our financing activities in fiscal 2015 for the purchase of stock under a stock repurchase plan during fiscal 2015.

We generated \$1.1 million in cash from our financing activities from continuing operations in fiscal 2014, which is a result of the issuance of common stock for the exercise of employee stock options.

Debt Instruments and Related Covenants

We renewed our letter agreement for a demand discretionary line of credit and a demand promissory note in the aggregate amount of \$20.0 million, effective November 26, 2014. Borrowings under the line of credit will be used to finance working capital needs and for general corporate purposes. We currently do not have any borrowings nor are there any financial covenants under this line.

Contractual Obligations

The following table reflects our current and contingent contractual obligations to make potential future payments as of January 31, 2015:

	Total	Less than one year	One to three years	Three to five years	Over five years
	(Amounts in thousands)				
Purchase obligations(1)	\$ 5,280	\$ 5,280	\$	\$	\$
Non-cancelable lease obligations	4,448	2,261	2,187		
Total	\$ 9,728	\$ 7,541	\$ 2,187	\$	\$

- (1) Represents obligations under agreements with non-cancelable terms to purchase goods or services. The agreements are enforceable and legally binding, and specify terms, including quantities to be purchased and the timing of the purchase.

We have excluded from the table above uncertain tax liabilities as defined by authoritative guidance due to the uncertainty of the amount and period of payment. As of January 31, 2015, we have gross unrecognized tax benefits of \$5.5 million.

Under the purchase agreement pursuant to which we acquired Timeline Labs on February 2, 2015, the Company is obligated to make earnout payments totaling up to \$2.5 million, payable in shares of our common stock, measured by qualifying revenue, on a cumulative and one-year performance target basis for the fiscal years ended January 31, 2016 and 2017.

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Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements as defined in Item 303(a)(4)(ii) of Regulation S-K.

Critical Accounting Policies and Significant Judgments and Estimates

Our consolidated financial statements are prepared in accordance with U.S. GAAP, which requires management to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses and disclosure of contingent assets and liabilities. Our actual results could differ from these estimates under different assumptions and conditions.

The significant accounting policies and methods used in the preparation of our consolidated financial statements are described in Note 2., *Summary of Significant Accounting Policies*, to our consolidated financial statements set forth in Part II, Item 8, of this Form 10-K. We believe the following critical accounting policies reflect the significant estimates, judgments and assumptions used in the preparation of our consolidated financial statements.

Principles of Consolidation

We consolidate the financial statements of our wholly-owned subsidiaries and all inter-company accounts are eliminated in consolidation. We also hold minority investments in the capital stock of certain private companies having product offerings or customer relationships that have strategic importance. We evaluate our equity and debt investments and other contractual relationships with affiliate companies in order to determine whether the guidelines regarding the consolidation of Variable Interest Entities (VIE) should be applied in the financial statements. Consolidation guidelines address consolidation by business enterprises of variable interest entities that possess certain characteristics. A VIE is defined as an entity in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. The primary beneficiary is required to consolidate the financial position and results of the VIE. We have concluded that we are not the primary beneficiary for any variable interest entities as of January 31, 2015.

Our investments in affiliates include investments accounted for under the cost method and the equity method of accounting. The investments that represent less than a 20% ownership interest of the common shares of the affiliate are carried at cost. Under the equity method of accounting, which generally applies to investments that represent 20% to 50% ownership of the common shares of the affiliate, our proportionate ownership share of the earnings or losses of the affiliate are included in equity income in earnings of affiliates in the consolidated statement of operations and comprehensive loss.

We periodically review indicators of the fair value of our investments in affiliates in order to assess whether available facts or circumstances, both internally and externally, may suggest an other-than-temporary decline in the value of the investment. The carrying value of an investment in an affiliate may be affected by the affiliate's ability to obtain adequate funding and execute its business plans, general market conditions, industry considerations specific to the affiliate's business, and other factors. The inability of an affiliate to obtain future funding or successfully execute its business plan could adversely affect our equity earnings of the affiliate in the periods affected by those events. Future adverse changes in market conditions or poor operating results of the affiliates could result in equity losses or an inability to recover the carrying value of the investments in affiliates that may not be reflected in an investment's current carrying value, thereby possibly requiring an impairment charge in the future. We record an impairment charge when we believe an investment has experienced a decline in value that is other-than-temporary.

Table of Contents***Revenue Recognition***

Our transactions frequently involve the sales of hardware, software, systems and services in multiple-element arrangements. Revenues from sales of hardware, software and systems that do not require significant modification or customization of the underlying software are recognized when:

persuasive evidence of an arrangement exists;

delivery has occurred, and title and risk of loss have passed to the customer;

fees are fixed or determinable; and

collection of the related receivable is considered probable.

Customers are billed for installation, training, project management and at least one year of product maintenance and technical support at the time of the product sale. Revenue from these activities is deferred at the time of the product sale and recognized ratably over the period these services are performed. Revenue from ongoing product maintenance and technical support agreements is recognized ratably over the period of the related agreements. Revenue from software development contracts that include significant modification or customization, including software product enhancements, is recognized based on the percentage of completion contract accounting method using labor efforts expended in relation to estimates of total labor efforts to complete the contract. Accounting for contract amendments and customer change orders are included in contract accounting when executed. Revenue from shipping and handling costs and other out-of-pocket expenses reimbursed by customers are included in revenues and cost of revenues. Our share of intercompany profits associated with sales and services provided to affiliated companies are eliminated in consolidation in proportion to our equity ownership.

Revenue from the sale of software-only products remains within the scope of the software revenue recognition rules. Maintenance and support, training, consulting, and installation services no longer fall within the scope of the software revenue recognition rules, except when they are sold with and relate to a software-only product. Revenue recognition for products that no longer fall under the scope of the software revenue recognition rules is similar to that for other tangible products and Accounting Standard Update No. (ASU) 2009-13, *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements*, amended ASC 605 and is applicable for multiple-deliverable revenue arrangements. ASU 2009-13 allows companies to allocate revenue in a multiple-deliverable arrangement in a manner that better reflects the transaction's economics.

Under the software revenue recognition rules, the fee is allocated to the various elements based on vendor-specific objective evidence (VSOE) of fair value. Under this method, the total arrangement value is allocated first to undelivered elements based on their fair values, with the remainder being allocated to the delivered elements. Where fair value of undelivered service elements has not been established, the total arrangement value is recognized over the period during which the services are performed. The amounts allocated to undelivered elements, which may include project management, training, installation, maintenance and technical support and certain hardware and software components, are based upon the price charged when these elements are sold separately and unaccompanied by the other elements. The amount allocated to installation, training and project management revenue is based upon standard hourly billing rates and the estimated time necessary to complete the service. These services are not essential to the

functionality of systems as these services do not alter the equipment's capabilities, are available from other vendors and the systems are standard products. For multiple-element arrangements that include software development with significant modification or customization and systems sales where VSOE of the fair value does not exist for the undelivered elements of the arrangement (other than maintenance and technical support), percentage of completion accounting is applied for revenue recognition purposes to the entire arrangement with the exception of maintenance and technical support.

Under the revenue recognition rules for tangible products as amended by ASU 2009-13, the fee from a multiple-deliverable arrangement is allocated to each of the deliverables based upon their relative selling prices as determined by a selling-price hierarchy. A deliverable in an arrangement qualifies as a separate unit of accounting if the delivered item has value to the customer on a stand-alone basis. A delivered item that does not

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qualify as a separate unit of accounting is combined with the other undelivered items in the arrangement and revenue is recognized for those combined deliverables as a single unit of accounting. The selling price used for each deliverable is based upon VSOE if available, third-party evidence (TPE) if VSOE is not available, and best estimate of selling price (BESP) if neither VSOE nor TPE are available. TPE is the price of the Company's, or any competitor's, largely interchangeable products or services in stand-alone sales to similarly situated customers. BESP is the price at which we would sell the deliverable if it were sold regularly on a stand-alone basis, considering market conditions and entity-specific factors.

The selling prices used in the relative selling price allocation method for certain of our services are based upon VSOE. The selling prices used in the relative selling price allocation method for third-party products from other vendors are based upon TPE. The selling prices used in the relative selling price allocation method for our hardware products, software, subscriptions, and customized services for which VSOE does not exist are based upon BESP. We do not believe TPE exists for these products and services because they are differentiated from competing products and services in terms of functionality and performance and there are no competing products or services that are largely interchangeable. Management establishes BESP with consideration for market conditions, such as the impact of competition and geographic considerations, and entity-specific factors, such as the cost of the product, discounts provided and profit objectives. Management believes that BESP is reflective of reasonable pricing of that deliverable as if priced on a stand-alone basis.

For our cloud and managed service revenues, we generate revenue from two sources: (1) subscription and support services; and (2) professional services and other. Subscription and support revenue includes subscription fees from customers accessing our cloud-based software platform and support fees. Our arrangements with customers do not provide the customer with the right to take possession of the software supporting the cloud-based software platform at any time. Professional services and other revenue include fees from implementation and customization to support customer requirements. 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. For the most part, subscription and support agreements are entered into for 12 to 36 months. Generally, a majority of the professional services component of the arrangements with customers is performed within a year of entering into a contract with the customer.

In most instances, revenue from a new customer acquisition is generated under sales agreements with multiple elements, comprised of subscription and support and other professional services. We evaluate each element in a multiple-element arrangement to determine whether it represents a separate unit of accounting. An element constitutes a separate unit of accounting when the delivered item has standalone value and delivery of the undelivered element is probable and within our control.

In determining when to recognize revenue from a customer arrangement, we are often required to exercise judgment regarding the application of our accounting policies to a particular arrangement. The primary judgments used in evaluating revenue recognized in each period involve: determining whether collection is probable, assessing whether the fee is fixed or determinable, and determining the fair value of the maintenance and service elements included in multiple-element software arrangements. Such judgments can materially impact the amount of revenue that we record in a given period. While we follow specific and detailed rules and guidelines related to revenue recognition, we make and use significant management judgments and estimates in connection with the revenue recognized in any reporting period, particularly in the areas described above. If management made different estimates or judgments, material differences in the timing of the recognition of revenue could occur.

Allowance for Doubtful Accounts

We recognize revenue for products and services only in those situations where collection from the customer is probable. We perform ongoing credit evaluations of customers' financial condition but generally do not require collateral. For some international customers, we may require an irrevocable letter of credit to be issued by the

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customer before the purchase order is accepted. We monitor payments from customers and assess any collection issues. We maintain allowances for specific doubtful accounts and other risk categories of accounts based on estimates of losses resulting from the inability of our customers to make required payments and record these allowances as a charge to general and administrative expenses. We base our allowances for doubtful accounts on historical collections and write-off experience, current trends, credit assessments, and other analysis of specific customer situations. While such credit losses have historically been within our expectations and the allowances established, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past. If the financial condition of our customers were to change, additional allowances may be required or established allowances may be considered unnecessary. Judgment is required in making these determinations and our failure to accurately estimate the losses for doubtful accounts and ensure that payments are received on a timely basis could have a material adverse effect on our business, financial condition and results of operations.

Fair Value Measurements

We measure certain financial assets and liabilities at fair value based on valuation techniques using the best information available, which may include quoted market prices, market comparables and discounted cash flow projections. Financial instruments include money market funds, corporate debt investments, asset-backed securities, government-sponsored enterprises and state municipal obligations.

In general, and where applicable, we use quoted prices in active markets for identical assets or liabilities to determine fair value. If quoted prices in active markets for identical assets or liabilities are not available to determine fair value, then we use quoted prices for similar assets and liabilities or inputs that are observable either directly or indirectly.

Inventories and Reserves

Inventories are stated at the lower of cost or net realizable value. Cost is determined using the first-in, first-out (FIFO) method. Inventories consist primarily of components and subassemblies and finished products held for sale. All of our hardware components are purchased from outside vendors. The value of inventories is reviewed quarterly to determine that the carrying value is stated at the lower of cost or net realizable value. We record charges to reduce inventory to its net realizable value when impairment is identified through the quarterly review process. The obsolescence evaluation is based upon assumptions and estimates about future demand and possible alternative uses and involves significant judgments.

Accounting for Business Combinations

We apply the acquisition method of accounting for business combinations, including our acquisition of Timeline Labs on February 2, 2015. Under this method of accounting, we are required to record the assets acquired, liabilities assumed, contractual contingencies, and contingent consideration at their fair value on the acquisition date. Determining these fair values and completing the purchase price allocation process requires management to make significant estimates and assumptions, especially at acquisition date with respect to intangible assets, estimated contingent consideration payments and pre-acquisition contingencies. Any excess of the purchase price over the fair value of the net assets acquired is recognized as goodwill. Although we believe the assumptions and estimates we have made have been reasonable and appropriate, they are based in part on historical experience and information obtained from the management of the acquired company and are inherently uncertain. Examples of critical estimates in accounting for acquisitions include but are not limited to:

the estimated fair value of the acquisition-related contingent consideration, which is calculated using a probability-weighted discounted cash flow model based upon the forecasted achievement of post acquisition bookings targets;

the future expected cash flows from product sales, support agreements, consulting contracts, other customer contracts and acquired developed technologies and patents; and

the relevant discount rates.

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Unanticipated events and circumstances may occur which may affect the accuracy or validity of such assumptions, estimates or actual results. 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 assets acquired and liabilities assumed with the corresponding offset to goodwill. Additionally, any change in the fair value of the acquisition-related contingent consideration subsequent to the acquisition date, including changes from events after the acquisition date, such as changes in our estimate of the bookings that are expected to be achieved, will be recognized in earnings in the period of the estimated fair value change. A change in fair value of the acquisition-related contingent consideration could have a material effect on the statement of operations and financial position in the period of the change in estimate.

Acquired Intangible Assets and Goodwill***Acquired Intangible Assets***

We use significant judgment in determining the fair value of acquired intangible assets, whether the assets are amortizable or non-amortizable and the period and method by which the intangible asset will be amortized. Intangible assets include customer contracts, completed technology, non-compete agreements, trademarks and patents. Acquired intangible assets are reported at cost, net of accumulated amortization and are either amortized on a straight-line basis over their estimated useful lives during the period the economic benefits of the intangible asset are consumed or otherwise used up. We review definite-lived intangible assets for impairment when indication of a potential impairment exists.

Goodwill

In connection with acquisitions of operating entities, we recognize the excess of the purchase price over the fair value of the net assets acquired as goodwill. Goodwill is not amortized, but is evaluated for impairment at least annually, in our third quarter beginning August 1st. Goodwill may be required to be tested for impairment on an interim basis in addition to the annual evaluation, if an event occurs or circumstances change. We monitor economic, legal and other factors as a whole between annual impairment tests to ensure that there are no indicators that make it more likely than not that there has been a decline in our fair value below our carrying value, indicating that the recorded goodwill may be impaired. We test goodwill for impairment by evaluating our fair value compared to the book value. If the book value of the Company exceeds its fair value, the implied fair value of goodwill is compared to the carrying amount of goodwill. If the carrying amount of goodwill exceeds the implied fair value, an impairment loss is recorded in an amount equal to that excess.

Long-Lived Assets

We review property and equipment, investments and other long-lived assets on a regular basis for impairment when indication of potential impairment exists. If such circumstances exist, we evaluate the carrying value of long-lived assets to determine if impairment exists based upon estimated undiscounted future cash flows over the remaining useful life of the assets and compare that value to the carrying value of the assets. Our cash flow estimates contain management's best estimates, using appropriate and customary assumptions and projections at the time.

Internal Use Software

Certain costs incurred in the application development phase of software development for internal use are capitalized and amortized over the product's estimated useful life, which is three years. The Company expenses all costs incurred that relate to planning and post implementation phases of development. Capitalized costs related to internally developed software under development are treated as construction in progress until the technology is available for

intended use, at which time the amortization commences. The Company capitalized internally developed software costs of \$0.5 million in fiscal 2015. Maintenance and training costs are expensed as incurred.

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Software Development Costs

We also purchase software for resale and capitalize those costs associated with projects that meet technological feasibility. Amortization expense of capitalized software is recorded over the period of economic consumption or the life of the agreement, whichever results in the higher expense, starting with the first shipment of the product to a customer. Amortization expense of capitalized software was immaterial for fiscal 2015 and 2014, and \$0.7 million for fiscal 2013.

Accounting for Income Taxes

Income tax comprises current and deferred tax. Income tax is recognized in the consolidated statements of operations and comprehensive loss except to the extent that it relates to items recognized directly within equity or in other comprehensive loss. Income taxes payable, which is included in other accrued expenses in our consolidated balance sheets, is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially-enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax assets and liabilities are recognized, using the balance sheet method, for the expected tax consequences of temporary differences between the carrying amounts of assets and liabilities and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets and liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantially-enacted by the reporting date.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income in the countries where the deferred tax assets originated and during the periods when the deferred tax assets become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment.

We operate in multiple jurisdictions with complex tax policy and regulatory environments. In certain of these jurisdictions, we may take tax positions that management believes are supportable, but are potentially subject to successful challenge by the applicable taxing authority. These interpretational differences with the respective governmental taxing authorities can be impacted by the local economic and fiscal environment. We evaluate our tax positions and establish liabilities in accordance with the applicable accounting guidance on uncertainty in income taxes. We review these tax uncertainties in light of changing facts and circumstances, such as the progress of tax audits, and adjust them accordingly. We have a number of audits in process in various jurisdictions. Although the resolution of these tax positions is uncertain, based on currently available information, we believe that the ultimate outcomes will not have a material adverse effect on our financial position, results of operations or cash flows.

Because there are a number of estimates and assumptions inherent in calculating the various components of our tax provision, certain changes or future events such as changes in tax legislation, geographic mix of earnings, completion of tax audits or earnings repatriation plans could have an impact on those estimates and our effective tax rate.

Stock-based Compensation

We account for all employee and non-employee director stock-based compensation awards using the authoritative guidance regarding share-based payments. We continue to use the Black-Scholes pricing model as we feel it is the most appropriate method for determining the estimated fair value of the majority of applicable

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awards. We also use the Monte Carlo pricing model for our market-based option awards. Determining the appropriate fair value model and calculating the fair value of share-based payment awards requires the input of highly subjective assumptions, including the expected life of the share-based payment awards and stock price volatility. Management estimates the volatility based on the historical volatility of our stock. The assumptions used in calculating the fair value of share-based payment awards represent management's best estimates, but these estimates involve inherent uncertainties and the application of management's judgment. As a result, if circumstances change and we use different assumptions, our stock-based compensation expense could be materially different in the future. In addition, we are required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. If our actual forfeiture rate is materially different from our estimate, the stock-based compensation expense could be significantly different from what we have recorded in the current period. The estimated fair value of our stock-based options and performance-based restricted stock units (RSUs), less expected forfeitures, is amortized over the awards vesting period on a graded vesting basis, whereas the RSUs are amortized on a straight-line basis.

Foreign Currency Translation

For subsidiaries where the U.S. dollar is designated as the functional currency of the entity, we translate that entity's monetary assets and liabilities denominated in local currencies into U.S. dollars (the functional and reporting currency) at current exchange rates, as of each balance sheet date. Non-monetary assets (e.g., inventories, property, plant, and equipment and intangible assets) and related income statement accounts (e.g., cost of sales, depreciation, amortization of intangible assets) are translated at historical exchange rates between the functional currency (the U.S. dollar) and the local currency. Revenue and other expense items are translated using average exchange rates during the fiscal period. Translation adjustments resulting from translation of the subsidiaries' accounts are included in accumulated other comprehensive loss, a separate component of stockholders' equity. Gains and losses resulting from foreign currency transactions, and any unrealized gains and losses on short-term inter-company transactions are included in other income or expense, net.

For subsidiaries where the local currency is designated as the functional currency, we translate the subsidiaries' assets and liabilities into U.S. dollars (the reporting currency) at current exchange rates as of each balance sheet date. Revenue and expense items are translated using average exchange rates during the period. Cumulative translation adjustments are presented as a separate component of stockholders' equity. Exchange gains and losses on foreign currency transactions and unrealized gains and losses on short-term inter-company transactions are included in other expense, net.

The aggregate foreign exchange transaction losses included as other expense, net, on the consolidated statement of operations and comprehensive loss was \$2.3 million, \$0.4 million and approximately \$23,000 for the years ended January 31, 2015, 2014 and 2013, respectively.

Recent Accounting Pronouncements

We consider the applicability and impact of all Accounting Standards Updates. Updates not listed below were assessed and determined to be either not applicable or are expected to have minimal impact on our consolidated financial position or results of operations.

Recent Accounting Guidance Not Yet Effective***Amendments to the Consolidation Analysis***

In February 2015, the Financial Accounting Standards Board (FASB) issued ASU 2015-02, *Amendments to the Consolidation Analysis*. ASU 2015-02 is intended to improve guidance for limited partnerships, limited liability corporations and securitization structures. The guidance places more emphasis on risk of loss when determining a controlling financial interest, reduces the frequency of the application of related-party guidance when determining a controlling financial interest in a VIE and changes consolidation conclusions for public and

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private companies that typically make use of limited partnerships or VIEs. This guidance is effective for us beginning in fiscal 2017. Early adoption is permitted. We are currently evaluating the impact of the adoption of ASU 2015-02 on our consolidated financial statements.

Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Item

In January 2015, FASB issued ASU 2015-01, *Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Item*. ASU 2015-01 is meant to reduce complexity in accounting standards by eliminating the concept of extraordinary items from U.S. GAAP. In the event of a transaction that meets the criteria for extraordinary classification, an entity is required to segregate the extraordinary item from the results of ordinary operations and show the item separately in the income statement, net of tax after income from continuing operations. This new guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. A reporting entity may apply the amendments prospectively. A reporting entity also may apply the amendments retrospectively to all prior periods presented in the financial statements. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. Besides presentation on the consolidated statements of operations and comprehensive loss when an item that meets the extraordinary criteria exists, we do not feel that adoption of ASU 2015-01 will have a material impact on our consolidated financial statements.

Accounting For Share-Based Payments-Performance Target Could Be Achieved after the Requisite Service Period

In June 2014, FASB issued ASU 2014-12, *Compensation Stock Compensation (Topic 718) Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period*. ASU 2014-12 requires that a performance target which affects vesting and that could be achieved after the requisite service period be treated as a performance condition by applying existing guidance in Topic 718 as it relates to awards with performance conditions. The amendment also specifies the period over which compensation costs should be recognized. The amendment is effective for annual reporting periods and interim periods within those annual periods beginning after December 15, 2015. Early adoption is permitted. We are currently evaluating the impact of the adoption of ASU 2014-12 on our consolidated financial statements.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and the International Financial Reporting Standards. This guidance supersedes previously issued guidance on revenue recognition and gives a five step process an entity should follow so that the entity recognizes revenue that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This new guidance will be effective for our fiscal 2018 reporting period and must be applied either retrospectively during each prior reporting period presented or retrospectively with the cumulative effect of initially applying this guidance recognized at the date of the initial application. Early adoption is not permitted. We are currently evaluating the impact of the adoption of this ASU on our consolidated financial statements.

Reporting Discontinued Operations and Disposals of Components of an Entity

In April 2014, the FASB issued ASU 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360) Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*, which changes the criteria for reporting discontinued operations while enhancing disclosures in this area.

The amended guidance requires that a disposal representing a strategic shift that has (or will have) a major effect on an entity's financial results or a business activity classified as held for sale should be

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reported as discontinued operations. This guidance also expands the disclosures required when an entity reports a discontinued operation or when it disposes of or classifies as held for sale an individually significant component that does not meet the definition of a discontinued operation. This new guidance will be effective prospectively on disposals (or classifications of held for sale) of components of an entity that occur within our fiscal year beginning on February 1, 2015. Early adoption is permitted but only for disposals (or classification as held for sale) that have not been reported in financial statements previously issued or available for issuance. We do not anticipate material impacts on our financial statements upon initial adoption. This guidance could have a material impact on our disclosure requirements if we dispose of, or classify as held for sale, an individually significant component of our business that does not meet the definition of a discontinued operation.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exchange Rate Risk

We face exposure to financial market risks, including adverse movements in foreign currency exchange rates and changes in interest rates. These exposures may change over time as business practices evolve and could have a material adverse impact on our financial results. Our foreign currency exchange exposure is primarily associated with product sales arrangements or settlement of intercompany payables and receivables among subsidiaries and their respective parent company, and/or investment/equity contingency considerations denominated in the local currency where the functional currency of the foreign subsidiary is the U.S. dollar.

Our principal currency exposures relate primarily to the U.S. dollar, the Euro and the Philippine peso. All foreign currency gains and losses are included in other expenses, net, in the accompanying consolidated statements of operations and comprehensive loss. For fiscal 2015 we recorded approximately \$2.3 million in losses due to the international subsidiary translations and cash settlements of revenues and expenses.

In addition, because a substantial portion of our earnings are generated by our foreign subsidiaries whose functional currency are other than the U.S. dollar, our earnings could be materially impacted by movements in foreign currency exchange rates upon the translation of the subsidiary's earnings into the U.S. dollar. If the U.S. dollar had been stronger by 10% compared to the Euro, our total revenues would have decreased by \$3.3 million and would have negatively impacted our operations by \$0.3 million.

Interest Rate Risk

Exposure to market risk for changes in interest rates relates primarily to our investment portfolio of marketable debt securities of various issuers, types and maturities and to our borrowings under our demand note payable. We do not use derivative instruments in our investment portfolio, and our investment portfolio only includes highly liquid instruments. Our cash and marketable securities include cash equivalents, which we consider to be investments purchased with original maturities of 90 days or less. There is risk that losses could be incurred if we were to sell any securities prior to stated maturity. Given the short maturities and investment grade quality of the portfolio holdings at January 31, 2015, a hypothetical 10% adverse movement in interest rates should not have a material adverse impact on the fair value of our investment portfolio. However, our long-term marketable securities, which are carried at the lower of cost or market value, have fixed interest rates, and therefore are subject to changes in fair value due to changes in interest rates.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of SeaChange International, Inc.

We have audited the accompanying consolidated balance sheets of SeaChange International, Inc. (a Delaware corporation) and subsidiaries (the Company) as of January 31, 2015 and 2014, and the related consolidated statements of operations and comprehensive loss, cash flows and stockholders' equity for each of the three years in the period ended January 31, 2015. Our audits of the basic consolidated financial statements included the financial statement schedule listed in the index appearing under Item 15(a)(2). These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of SeaChange International, Inc. and subsidiaries as of January 31, 2015 and 2014, and the results of their operations and their cash flows for each of the three years in the period ended January 31, 2015 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of January 31, 2015, based on criteria established in the 2013 *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated April 7, 2015 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

Boston, Massachusetts

April 7, 2015

Table of Contents**SEACHANGE INTERNATIONAL, INC.****CONSOLIDATED BALANCE SHEETS****(Amounts in thousands, except share data)**

	January 31, 2015	January 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	\$ 90,019	\$ 115,734
Restricted cash	1,073	
Marketable securities	7,516	5,555
Accounts and other receivables, net of allowance for doubtful accounts of \$400 and \$327 at January 31, 2015 and January 31, 2014, respectively	24,962	30,203
Unbilled receivables	6,588	5,511
Inventories, net	2,864	6,632
Prepaid expenses and other current assets	3,026	5,242
Total current assets	136,048	168,877
Property and equipment, net	15,869	18,530
Marketable securities, long-term	6,793	6,814
Investments in affiliates	3,051	1,051
Intangible assets, net	7,314	12,855
Goodwill	41,008	45,150
Other assets	2,268	836
Total assets	\$ 212,351	\$ 254,113
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 5,129	\$ 6,640
Other accrued expenses	12,507	12,332
Deferred revenues	17,398	24,030
Total current liabilities	35,034	43,002
Deferred revenue, long-term	1,690	1,598
Other liabilities, long-term	1,493	936
Taxes payable, long-term	1,993	2,503
Deferred tax liabilities, long-term	1,090	1,633
Total liabilities	41,300	49,672
Commitments and contingencies (Note 8)		
Stockholders equity:		
	327	330

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Common stock, \$0.01 par value; 100,000,000 shares authorized; 32,733,636 shares issued and 32,693,852 outstanding at January 31, 2015, and 33,037,671 shares issued and 32,997,887 outstanding at January 31, 2014		
Additional paid-in capital	219,651	221,932
Treasury stock, at cost; 39,784 common shares	(1)	(1)
Accumulated loss	(43,172)	(15,688)
Accumulated other comprehensive loss	(5,754)	(2,132)
Total stockholders' equity	171,051	204,441
Total liabilities and stockholders' equity	\$ 212,351	\$ 254,113

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

Table of Contents**SEACHANGE INTERNATIONAL, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS****(Amounts in thousands, except per share data)**

	For the Fiscal Years Ended January 31,		
	2015	2014	2013
Revenues:			
Products	\$ 31,507	\$ 54,749	\$ 64,274
Services	83,928	91,570	92,914
Total revenues	115,435	146,319	157,188
Cost of revenues:			
Products	8,845	10,526	17,397
Services	48,272	55,075	52,162
Amortization of intangible assets	1,070	1,269	2,429
Stock-based compensation expense	141	250	157
Inventory write-down			1,752
Total cost of revenues	58,328	67,120	73,897
Gross profit	57,107	79,199	83,291
Operating expenses:			
Research and development	42,169	39,657	38,667
Selling and marketing	13,920	15,018	15,398
General and administrative	16,014	17,618	17,674
Amortization of intangible assets	4,084	3,361	3,966
Stock-based compensation expense	3,079	2,709	5,772
Earn-outs and change in fair value of earn-outs		(60)	2,435
Professional fees other	671	1,614	1,619
Severance and other restructuring costs	3,623	911	3,106
Total operating expenses	83,560	80,828	88,637
Loss from operations	(26,453)	(1,629)	(5,346)
Other expenses, net	(2,161)	(224)	(86)
(Loss) gain on sale of investment in affiliates		(363)	885
Loss before income taxes and equity income in earnings of affiliates	(28,614)	(2,216)	(4,547)
Income tax (benefit) provision	(1,106)	55	(1,555)

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Equity income in earnings of affiliates, net of tax	19	44	193
Loss from continuing operations	(27,489)	(2,227)	(2,799)
Loss on sale of discontinued operations			(14,073)
Income (loss) from discontinued operations, net of tax	5	(803)	(2,293)
Net loss	\$ (27,484)	\$ (3,030)	\$ (19,165)
Net loss	\$ (27,484)	\$ (3,030)	\$ (19,165)
Other comprehensive loss, net of tax:			
Foreign currency translation adjustment	(3,647)	(294)	7,954
Unrealized gain (loss) on marketable securities(1)	25	(12)	(6)
Comprehensive loss	\$ (31,106)	\$ (3,336)	\$ (11,217)

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	For the Fiscal Years Ended January 31,		
	2015	2014	2013
Loss per share:			
Basic loss per share	\$ (0.84)	\$ (0.09)	\$ (0.59)
Diluted loss per share	\$ (0.84)	\$ (0.09)	\$ (0.59)
Loss per share from continuing operations:			
Basic loss per share	\$ (0.84)	\$ (0.07)	\$ (0.09)
Diluted loss per share	\$ (0.84)	\$ (0.07)	\$ (0.09)
Income (loss) per share from discontinued operations:			
Basic loss per share	\$ 0.00	\$ (0.02)	\$ (0.50)
Diluted loss per share	\$ 0.00	\$ (0.02)	\$ (0.50)
Weighted average common shares outstanding:			
Basic	32,772	32,718	32,494
Diluted	32,772	32,718	32,494

(1) Tax amounts for all periods were not significant

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

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SEACHANGE INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands)

	For the Fiscal Years Ended January 31,		
	2015	2014	2013
Cash flows from operating activities:			
Net loss	\$ (27,484)	\$ (3,030)	\$ (19,165)
Net (income) loss from discontinued operations	(5)	803	16,366
Adjustments to reconcile net loss to net cash (used in) provided by continuing operating activities:			
Depreciation and amortization of property and equipment	3,683	4,389	4,671
Amortization of intangible assets	5,154	4,630	6,395
Stock-based compensation expense	3,220	2,959	5,929
Deferred income taxes	(372)	(684)	(132)
Other	512	798	2,596
Changes in operating assets and liabilities:			
Accounts receivable	3,567	5,420	1,676
Unbilled receivables	(1,993)	(5,251)	4,637
Inventories	3,183	(234)	2,563
Prepaid expenses and other assets	1,570	6,724	(5,045)
Accounts payable	(1,619)	(873)	(236)
Accrued expenses	1,650	(3,146)	1,430
Deferred revenues	(5,699)	(4,877)	(6,283)
Other	1,289	539	568
Net cash (used in) provided by operating activities from continuing operations	(13,344)	8,167	15,970
Net cash provided by (used in) operating activities from discontinued operations	5	(803)	1,387
Total cash (used in) provided by operating activities	(13,339)	7,364	17,357
Cash flows from investing activities:			
Purchases of property and equipment	(1,873)	(2,315)	(3,972)
Purchases of marketable securities	(9,193)	(11,479)	(15,642)
Proceeds from sale and maturity of marketable securities	7,181	12,237	14,214
Investment in affiliate	(2,000)		
Proceeds from sale of equity investment	229	1,128	885
Acquisition of businesses and payment of contingent consideration, net of cash acquired		(4,009)	(8,175)
Advance for Timeline Labs acquisition	(2,500)		
Other		958	452

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Net cash used in investing activities from continuing operations	(8,156)	(3,480)	(12,238)
Net cash provided by investing activities from discontinued operations		4,000	25,232
Total cash (used in) provided by investing activities	(8,156)	520	12,994

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	For the Fiscal Years Ended January 31,		
	2015	2014	2013
Cash flows from financing activities:			
Repurchases of our common stock	(5,504)		(6,200)
Proceeds from issuance of common stock relating to stock option exercises		1,058	2,191
Total cash provided by (used in) financing activities	(5,504)	1,058	(4,009)
Effect of exchange rate changes on cash	1,284	71	(206)
Net (decrease) increase in cash and cash equivalents	(25,715)	9,013	26,136
Cash and cash equivalents, beginning of period	115,734	106,721	80,585
Cash and cash equivalents, end of period	\$ 90,019	\$ 115,734	\$ 106,721
Supplemental disclosure of cash flow information:			
Income taxes paid	\$ 671	\$ 2,606	\$ 1,312
Interest paid	\$ 6	\$ 4	\$ 89
Supplemental disclosure of non-cash activities:			
Transfer of items originally classified as inventories to equipment	\$ 474	\$ 1,110	\$ 897
Issuance of common stock for settlement of contingent consideration related to acquisitions	\$	\$ 1,560	\$
Asset held for sale reclassified to asset held for use and reclassified from current assets to property and equipment	\$	\$ 465	\$

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

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SEACHANGE INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(Amounts in thousands, except share amounts)

	Common Stock		Accumulated Other Comprehensive Income (Loss)			Treasury Stock		Total Stockholders Equity	
	Number of Shares	Par Value	Additional Paid-In Capital	Accumulated Deficit	Translation Adjustment	Unrealized Gain/Loss Investments	Number of Shares		Amount
Balance at January 31, 2012	32,534,444	326	213,880	6,507	(9,810)	36	(39,784)	(1)	210,938
Issuance of common stock pursuant to exercise of stock options	304,550	2	2,189						2,191
Issuance of common stock pursuant to vesting of restricted stock units	359,676	4	(4)						
Issuance of common stock pursuant to deferred consideration	75,680	1	585						586
Purchase of treasury shares			(6,194)				(764,024)		(6,194)
Retirement of shares	(764,024)	(6)					764,024		(6)
Stock-based compensation expense			5,903						5,903
Change in fair value on marketable securities						(6)			(6)
Translation adjustment					7,954				7,954
Net loss				(19,165)					(19,165)

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Balance at January 31, 2013	32,510,326	327	216,359	(12,658)	(1,856)	30	(39,784)	(1)	202,201
Issuance of common stock pursuant to exercise of stock options	118,529	1	1,057						1,058
Issuance of common stock pursuant to vesting of restricted stock units	205,928	1	(1)						
Issuance of common stock pursuant to deferred consideration	202,888	1	1,558						1,559
Stock-based compensation expense			2,959						2,959
Change in fair value on marketable securities						(12)			(12)
Translation adjustment					(294)				(294)
Net loss				(3,030)					(3,030)

Balance at January 31, 2014	33,037,671	\$ 330	\$ 221,932	\$ (15,688)	\$ (2,150)	\$ 18	(39,784)	\$ (1)	\$ 204,441
Issuance of common stock pursuant to vesting of restricted stock units	287,485	3	(3)						
Purchase of treasury shares			(5,498)				(591,520)		(5,498)
Retirement of shares	(591,520)	(6)					591,520		(6)
Stock-based compensation expense			3,220						3,220
Change in fair value on marketable securities						25			25

Translation adjustment					(3,647)					(3,647)
Net loss					(27,484)					(27,484)

Balance at January 31, 2015	32,733,636	\$ 327	\$ 219,651	\$ (43,172)	\$ (5,797)	\$ 43	(39,784)	\$ (1)	\$ 171,051
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The accompanying notes are an integral part of these consolidated financial statements.

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SEACHANGE INTERNATIONAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Nature of Business

We are an industry leader in the delivery of multiscreen video. Our products and services facilitate the aggregation, licensing, management and distribution of video (primarily movies and television programming) and television advertising content to cable system operators, telecommunications companies and mobile communications providers.

2. Summary of Significant Accounting Policies

Significant accounting policies followed in the preparation of the accompanying consolidated financial statements are as follows:

Basis of Presentation and Principles of Consolidation

The accompanying consolidated financial statements have been prepared in accordance with U.S. GAAP. We consolidate the financial statements of our wholly-owned subsidiaries and all intercompany transactions and account balances have been eliminated in consolidation. We have reclassified certain prior fiscal year data to conform to our current fiscal year presentation.

We also hold minority investments in the capital stock of certain private companies having product offerings or customer relationships that have strategic importance. We evaluate our equity and debt investments and other contractual relationships with affiliate companies in order to determine whether the guidelines regarding the consolidation of VIEs should be applied in the financial statements. Consolidation guidelines address consolidation by business enterprises of VIEs that possess certain characteristics. A VIE is defined as an entity in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. We use qualitative analysis to determine whether or not we are the primary beneficiary of a VIE. We consider the rights and obligations conveyed by the implicit and explicit variable interest in each VIE and the relationship of these with the variable interests held by other parties to determine whether its variable interests will absorb a majority of a VIE's expected losses, receive a majority of its expected residual returns, or both. If we determine that our variable interests will absorb a majority of the VIE's expected losses, receive a majority of their expected residual returns, or both, we consolidate the VIE as the primary beneficiary, and if not, it is not consolidated. We have concluded that we are not the primary beneficiary for any variable interest entities during fiscal 2015.

Use of Estimates

The preparation of these financial statements in conformity with U.S. GAAP requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosure of contingent assets and liabilities. On an ongoing basis, management evaluates these estimates and judgments, including those related to the timing and amounts of revenue recognition, valuation of inventory, collectability of accounts receivable, valuation of investments and income taxes, assumptions used to determine stock-based compensation, valuation of goodwill and intangible assets and related amortization. Management bases these estimates on historical and anticipated results and trends and on various other assumptions that management believes are reasonable under the circumstances, including assumptions as to future events. These estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. By their nature,

estimates are subject to an inherent degree of uncertainty. Actual results may differ from management's estimates.

Table of Contents***Cash and Cash Equivalents***

Cash and cash equivalents include cash on hand and on deposit and highly liquid, temporary cash investments with an original maturity of three months or less. All cash equivalents are carried at cost, which approximates fair value.

Marketable Securities

We account for investments in accordance with authoritative guidance that defines investment classifications. We determine the appropriate classification of debt securities at the time of purchase and reevaluate such designation as of each balance sheet date. Our investment portfolio consists primarily of money market funds, U.S. treasury notes or bonds and U.S. government agency bonds at January 31, 2015 and 2014, but can consist of corporate debt investments, asset-backed securities and government-sponsored enterprises. Our marketable securities are classified as available-for-sale and are reported at fair value with unrealized gains and losses, net of tax, reported in stockholders equity as a component of accumulated other comprehensive loss. The amortization of premiums and accretion of discounts to maturity are computed under the effective interest method and are included in other expenses, net in our consolidated statements of operations and comprehensive loss. Interest on securities is recorded as earned and is also included in other expenses, net. Any realized gains or losses would be shown in the accompanying consolidated statements of operations and comprehensive loss in other expenses, net.

We evaluate our investments on a regular basis to determine whether an other-than-temporary decline in fair value has occurred. This evaluation consists of a review of several factors, including, but not limited to: the length of time and extent that an investment has been in an unrealized loss position; the existence of an event that would impair the issuer's future earnings potential; and our intent and ability to hold an investment for a period of time sufficient to allow for any anticipated recovery in fair value. Declines in value below cost for investments where it is considered probable that all contractual terms of the investment will be satisfied, are due primarily to changes in interest rates, and where the company has the intent and ability to hold the investment for a period of time sufficient to allow a market recovery, are not assumed to be other-than-temporary. Any other-than-temporary declines in fair value are recorded in earnings and a new cost basis for the investment is established.

Fair Value Measurements***Definition and Hierarchy***

The applicable accounting guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The guidance establishes a framework for measuring fair value and expands required disclosure about the fair value measurements of assets and liabilities. This guidance requires us to classify and disclose assets and liabilities measured at fair value on a recurring basis, as well as fair value measurements of assets and liabilities measured on a non-recurring basis in periods subsequent to initial measurement, in a fair value hierarchy.

The fair value hierarchy is broken down into three levels based on the reliability of inputs and requires an entity to maximize the use of observable inputs, where available. The following summarizes the three levels of inputs required, as well as the assets and liabilities that we value using those levels of inputs:

Level 1 Observable inputs that reflect quoted prices for identical assets or liabilities in active markets.

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not very active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. The fair value measurements of the contingent consideration obligations related to our business acquisitions are valued using Level 3 inputs.

Table of Contents*Valuation Techniques*

Inputs to valuation techniques are observable and unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our market assumptions. When developing fair value estimates for certain financial assets and liabilities, we maximize the use of observable inputs and minimize the use of unobservable inputs. When available, we use quoted market prices, market comparables and discounted cash flow projections. Financial instruments include money market funds, U.S. treasury notes or bonds and U.S. government agency bonds.

In general, and where applicable, we use quoted prices in active markets for identical assets or liabilities to determine fair value. If quoted prices in active markets for identical assets or liabilities are not available to determine fair value, then we use quoted prices for similar assets and liabilities or inputs that are observable either directly or indirectly. In periods of market inactivity, the observability of prices and inputs may be reduced for certain instruments. This condition could cause an instrument to be reclassified from Level 1 to Level 2 or from Level 2 to Level 3.

Concentration of Credit Risk

Financial instruments which potentially expose us to concentrations of credit risk include cash equivalents, investments in treasury bills, certificates of deposits and commercial paper, trade accounts receivable, accounts payable and accrued liabilities. We have cash investment policies which, among other things, limit investments to investment-grade securities. We restrict our cash equivalents and investments in marketable securities to repurchase agreements with major banks and U.S. government and corporate securities which are subject to minimal credit and market risk. We perform ongoing credit evaluations of our customers. As of January 31, 2015, two customers represented more than 10% of consolidated accounts receivable compared to one customer as of January 31, 2014. For fiscal 2015, 2014 and 2013, two, three and two customers each accounted for more than 10% of our total revenue.

Accounts Receivable and Allowances for Doubtful Accounts

For trade accounts receivable, we evaluate customers' financial condition, require advance payments from certain of our customers and maintain reserves for potential credit losses. We perform ongoing credit evaluations of customers' financial condition but generally do not require collateral. For some international customers, we require an irrevocable letter of credit to be issued by the customer before the purchase order is accepted. We monitor payments from customers and assess any collection issues. We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of the Company's customers to make required payments and record these allowances as a charge to general and administrative expenses in our consolidated statements of operations and comprehensive loss. We base our allowances for doubtful accounts on historical collections and write-off experience, current trends, credit assessments, and other analysis of specific customer situations. At January 31, 2015 and 2014, we had an allowance for doubtful accounts of \$0.4 million and \$0.3 million, respectively, to provide for potential credit losses. We charge off trade accounts receivables against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. Recoveries of trade receivables previously charged off are recorded when received.

Inventory Valuation

Inventories are stated at the lower of cost or net realizable value. Cost is determined using the first-in, first-out (FIFO) method. Inventories consist primarily of components and subassemblies and finished products held for sale. The values of inventories are reviewed quarterly to determine that the carrying value is stated at the lower of cost or net realizable value. We record charges to reduce inventory to its net realizable value when impairment is identified

through a quarterly review process. The obsolescence evaluation is based upon assumptions and

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estimates about future demand, or possible alternative uses and involves significant judgments. For the years ended January 31, 2015, 2014 and 2013, we recorded a provision for obsolescence of \$0.1 million, \$0.1 million and \$0.3 million, respectively.

Property and Equipment

Property and equipment consists of land and buildings, office and computer equipment, leasehold improvements, demonstration equipment, deployed assets and spare components and assemblies used to service our installed base. Property and equipment are recorded at cost and depreciated over their estimated useful lives. Determining the useful lives of property and equipment requires us to make significant judgments that can materially impact our operating results. If our estimates require adjustment, it could have a material impact on our reported results.

Demonstration equipment consists of systems manufactured by us for use in marketing and selling activities. Leasehold improvements are amortized over the shorter of their estimated useful lives or the term of the respective leases using the straight-line method. Deployed assets consist of movie systems owned and manufactured by us that are installed in a hotel environment. Deployed assets are depreciated over the life of the related service agreements. Capitalized service and spare components are depreciated over the estimated useful lives using the straight-line method. Maintenance and repair costs are expensed as incurred.

Generally, property and equipment include assets in service. Fully depreciated assets remaining in service along with related accumulated depreciation are not removed from the balance sheet until the corresponding asset is removed from service either through a retirement or sale. Upon retirement or sale of an asset or asset group, the cost of the assets disposed of, and the related accumulated depreciation, are removed from the accounts, and any resulting gain or loss is included in the determination of net income or loss.

Investments in Affiliates

Our investments in affiliates include investments accounted for under the cost method and the equity method of accounting. The investments that represent less than a 20% ownership interest of the common shares of the affiliate are carried at cost. Under the equity method of accounting, which generally applies to investments that represent 20% to 50% ownership of the common shares of the affiliate, our proportionate ownership share of the earnings or losses of the affiliate are included in equity income in earnings of affiliates in our consolidated statements of operations and comprehensive loss.

We periodically review indicators of the fair value of our investments in affiliates in order to assess whether available facts or circumstances, both internally and externally, may suggest an other than temporary decline in the value of the investment. If we determine that an other-than-temporary impairment has occurred, we will write-down the investment to its fair value. The carrying value of an investment in an affiliate may be affected by the affiliate's ability to obtain adequate funding and execute its business plans, general market conditions, the company's current cash position, earnings and cash flow forecasts, recent operational performance, and any other readily available data. The inability of an affiliate to obtain future funding or successfully execute its business plan could adversely affect our equity earnings of the affiliate in the periods affected by those events. Future adverse changes in market conditions or poor operating results of the affiliates could result in equity losses or an inability to recover the carrying value of the investments in affiliates that may not be reflected in an investment's current carrying value, thereby possibly requiring an impairment charge in the future.

Table of Contents***Intangible Assets and Goodwill***

Intangible assets consist of customer contracts, completed technology, non-compete agreements, trademarks and patents. The intangible assets are amortized to cost of sales and operating expenses, as appropriate, on a straight-line or accelerated basis, using the economic consumption life basis, in order to reflect the period that the assets will be consumed, which are:

Intangible assets with finite useful lives:

Customer contracts	1 - 8 years
Non compete agreements	2 - 3 years
Completed technology	4 - 6 years
Trademarks, patents and other	5 years

Goodwill is recorded when the consideration for an acquisition exceeds the fair value of net tangible and identifiable intangible assets acquired.

Impairment of Assets

Indefinite-lived intangible assets, such as goodwill are not amortized, but are evaluated for impairment, at the reporting unit level, annually in our third quarter beginning August 1st. Indefinite-lived intangible assets may be tested for impairment on an interim basis in addition to the annual evaluation if an event occurs or circumstances change such as declines in sales, earnings or cash flows, decline in the Company's stock price, or material adverse changes in the business climate, which would more likely than not reduce the fair value of a reporting unit below its carrying amount.

The process of evaluating indefinite-lived intangible assets for impairment requires several judgments and assumptions to be made to determine the fair value of the Company, including the method used to determine fair value, discount rates, expected levels of cash flows, revenues and earnings, and the selection of comparable companies used to develop market-based assumptions. We may employ one or more of three generally accepted approaches for valuing businesses: the market approach, the income approach and the asset-based (cost) approach to arrive at the fair value. We chose to use the market approach and the income approach to determine the value of the Company for our testing in fiscal 2015. In calculating the fair value, we derived the standalone projected five year cash flows for the Company. This process started with the projected cash flows which were discounted. The choice of which approach and methods to use in a particular situation depends on the facts and circumstances.

We also evaluate property and equipment, intangible assets with finite useful lives and other long-lived assets on a regular basis for the existence of facts or circumstances, both internal and external that may suggest an asset is not recoverable. If such circumstances exist, we evaluate the carrying value of long-lived assets to determine if impairment exists based upon estimated undiscounted future cash flows over the remaining useful life of the assets and compares that value to the carrying value of the assets. Our cash flow estimates contain management's best estimates, using appropriate and customary assumptions and projections at the time.

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Income Taxes

Income tax comprises current and deferred tax. Income tax is recognized in the consolidated statements of operations and comprehensive loss except to the extent that it relates to items recognized directly within equity or in other comprehensive loss. Income taxes payable, which is included in other accrued expenses in our consolidated balance sheets, is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially-enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax assets and liabilities are recognized, using the balance sheet method, for the expected tax consequences of temporary differences between the carrying amounts of assets and liabilities and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets and liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantially-enacted by the reporting date.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income in the countries where the deferred tax assets originated and during the periods when the deferred tax assets become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment.

We operate in multiple jurisdictions with complex tax policy and regulatory environments. In certain of these jurisdictions, we may take tax positions that management believes are supportable, but are potentially subject to successful challenge by the applicable taxing authority. These interpretational differences with the respective governmental taxing authorities can be impacted by the local economic and fiscal environment. We evaluate our tax positions and establish liabilities in accordance with the applicable accounting guidance on uncertainty in income taxes. We review these tax uncertainties in light of changing facts and circumstances, such as the progress of tax audits, and adjust them accordingly. We have a number of audits in process in various jurisdictions. Although the resolution of these tax positions is uncertain, based on currently available information, we believe that the ultimate outcomes will not have a material adverse effect on our financial position, results of operations or cash flows.

Because there are a number of estimates and assumptions inherent in calculating the various components of our tax provision, certain changes or future events such as changes in tax legislation, geographic mix of earnings, completion of tax audits or earnings repatriation plans could have an impact on those estimates and our effective tax rate.

Restructuring

Restructuring charges that we record consist of employee-related severance charges, contract termination costs and the disposal of related fixed assets. Restructuring charges represent our best estimate of the associated liability at the date the charges are recognized. Adjustments for changes in assumptions are recorded as a component of operating expenses in the period they become known. Differences between actual and expected charges and changes in assumptions could have a material effect on our restructuring accrual as well as our consolidated results of operations. See Note 7, *Severance and Other Restructuring Costs*, for more information on the current restructuring plan.

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Foreign Currency Translation

For subsidiaries where the U.S. dollar is designated as the functional currency of the entity, we translate that entity's monetary assets and liabilities denominated in local currencies into U.S. dollars (the functional and reporting currency) at current exchange rates, as of each balance sheet date. Non-monetary assets (e.g., inventories, property, plant, and equipment and intangible assets) and related income statement accounts (e.g., cost of sales, depreciation, amortization of intangible assets) are translated at historical exchange rates between the functional currency (the U.S. dollar) and the local currency. Revenue and other expense items are translated using average exchange rates during the fiscal period. Translation adjustments resulting from translation of the subsidiaries' accounts are included in accumulated other comprehensive loss, a separate component of stockholders' equity. Gains and losses on foreign currency transactions, and any unrealized gains and losses on short-term inter-company transactions are included in other expense, net.

For subsidiaries where the local currency is designated as the functional currency, we translate our assets and liabilities into U.S. dollars (the reporting currency) at current exchange rates as of each balance sheet date. Revenue and expense items are translated using average exchange rates during the period. Cumulative translation adjustments are presented as a separate component of stockholders' equity. Exchange gains and losses on foreign currency transactions and unrealized gains and losses on short-term inter-company transactions are included in other expense, net.

The aggregate foreign exchange transaction losses included in other expenses, net, on the consolidated statements of operations and comprehensive loss, were \$2.3 million, \$0.4 million and approximately \$23,000 for fiscal 2015, 2014 and 2013, respectively.

Comprehensive Loss

We present accumulated other comprehensive loss in our consolidated balance sheets and comprehensive loss in the consolidated statement of operations and comprehensive loss. At the end of fiscal 2015, 2014 and 2013, our comprehensive loss of \$31.1 million, \$3.3 million and \$11.2 million consists primarily of net loss, cumulative translation adjustments and unrealized gains and losses on marketable securities.

Revenue Recognition

Our transactions frequently involve the sales of hardware, software, systems and services in multiple-element arrangements. Revenues from sales of hardware, software and systems that do not require significant modification or customization of the underlying software are recognized when:

persuasive evidence of an arrangement exists;

delivery has occurred, and title and risk of loss have passed to the customer;

fees are fixed or determinable; and

collection of the related receivable is considered probable.

Customers are billed for installation, training, project management and at least one year of product maintenance and technical support at the time of the product sale. Revenue from these activities is deferred at the time of the product sale and recognized ratably over the period these services are performed. Revenue from ongoing product maintenance and technical support agreements is recognized ratably over the period of the related agreements. Revenue from software development contracts that include significant modification or customization, including software product enhancements, is recognized based on the percentage of completion contract accounting method using labor efforts expended in relation to estimates of total labor efforts to complete the contract. Accounting for contract amendments and customer change orders are included in contract accounting when executed. Revenue from shipping and handling costs and other out-of-pocket expenses reimbursed by customers are included in revenues and cost of revenues. Our share of intercompany profits associated with sales and services provided to affiliated companies are eliminated in consolidation in proportion to our equity ownership.

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Revenue from the sale of software-only products remains within the scope of the software revenue recognition rules. Maintenance and support, training, consulting, and installation services no longer fall within the scope of the software revenue recognition rules, except when they are sold with and relate to a software-only product. Revenue recognition for products that no longer fall under the scope of the software revenue recognition rules is similar to that for other tangible products and ASU 2009-13, *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements*, amended ASC 605 and is applicable for multiple-deliverable revenue arrangements. ASU 2009-13 allows companies to allocate revenue in a multiple-deliverable arrangement in a manner that better reflects the transaction's economics.

Under the software revenue recognition rules, the fee is allocated to the various elements based on vendor-specific objective evidence (VSOE) of fair value. Under this method, the total arrangement value is allocated first to undelivered elements based on their fair values, with the remainder being allocated to the delivered elements. Where fair value of undelivered service elements has not been established, the total arrangement value is recognized over the period during which the services are performed. The amounts allocated to undelivered elements, which may include project management, training, installation, maintenance and technical support and certain hardware and software components, are based upon the price charged when these elements are sold separately and unaccompanied by the other elements. The amount allocated to installation, training and project management revenue is based upon standard hourly billing rates and the estimated time necessary to complete the service. These services are not essential to the functionality of systems as these services do not alter the equipment's capabilities, are available from other vendors and the systems are standard products. For multiple-element arrangements that include software development with significant modification or customization and systems sales where VSOE of the fair value does not exist for the undelivered elements of the arrangement (other than maintenance and technical support), percentage of completion accounting is applied for revenue recognition purposes to the entire arrangement with the exception of maintenance and technical support.

Under the revenue recognition rules for tangible products as amended by ASU 2009-13, the fee from a multiple-deliverable arrangement is allocated to each of the deliverables based upon their relative selling prices as determined by a selling-price hierarchy. A deliverable in an arrangement qualifies as a separate unit of accounting if the delivered item has value to the customer on a stand-alone basis. A delivered item that does not qualify as a separate unit of accounting is combined with the other undelivered items in the arrangement and revenue is recognized for those combined deliverables as a single unit of accounting. The selling price used for each deliverable is based upon VSOE if available, third-party evidence (TPE) if VSOE is not available, and best estimate of selling price (BESP) if neither VSOE nor TPE are available. TPE is the price of the Company's, or any competitor's, largely interchangeable products or services in stand-alone sales to similarly situated customers. BESP is the price at which we would sell the deliverable if it were sold regularly on a stand-alone basis, considering market conditions and entity-specific factors.

The selling prices used in the relative selling price allocation method for certain of our services are based upon VSOE. The selling prices used in the relative selling price allocation method for third-party products from other vendors are based upon TPE. The selling prices used in the relative selling price allocation method for our hardware products, software, subscriptions, and customized services for which VSOE does not exist are based upon BESP. We do not believe TPE exists for these products and services because they are differentiated from competing products and services in terms of functionality and performance and there are no competing products or services that are largely interchangeable. Management establishes BESP with consideration for market conditions, such as the impact of competition and geographic considerations, and entity-specific factors, such as the cost of the product, discounts provided and profit objectives. Management believes that BESP is reflective of reasonable pricing of that deliverable as if priced on a stand-alone basis.

For our cloud and managed service revenues, we generate revenue from two sources: (1) subscription and support services; and (2) professional services and other. Subscription and support revenue includes subscription fees from customers accessing our cloud-based software platform and support fees. Our arrangements with customers do not provide the customer with the right to take possession of the software supporting the cloud-

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based software platform at any time. Professional services and other revenue include fees from implementation and customization to support customer requirements. 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. For the most part, subscription and support agreements are entered into for 12 to 36 months. Generally, a majority of the professional services component of the arrangements with customers is performed within a year of entering into a contract with the customer.

In most instances, revenue from a new customer acquisition is generated under sales agreements with multiple elements, comprised of subscription and support and other professional services. We evaluate each element in a multiple-element arrangement to determine whether it represents a separate unit of accounting. An element constitutes a separate unit of accounting when the delivered item has standalone value and delivery of the undelivered element is probable and within our control.

In determining when to recognize revenue from a customer arrangement, we are often required to exercise judgment regarding the application of our accounting policies to a particular arrangement. The primary judgments used in evaluating revenue recognized in each period involve: determining whether collection is probable, assessing whether the fee is fixed or determinable, and determining the fair value of the maintenance and service elements included in multiple-element software arrangements. Such judgments can materially impact the amount of revenue that we record in a given period. While we follow specific and detailed rules and guidelines related to revenue recognition, we make and use significant management judgments and estimates in connection with the revenue recognized in any reporting period, particularly in the areas described above. If management made different estimates or judgments, material differences in the timing of the recognition of revenue could occur.

Stock-based Compensation

We account for all employee and non-employee director stock-based compensation awards using the authoritative guidance regarding stock-based payments. We have continued to use the Black-Scholes pricing model as the most appropriate method for determining the estimated fair value of all applicable awards. We also use the Monte Carlo pricing model for our market-based option awards. Determining the appropriate fair value model and calculating the fair value of stock-based payment awards requires the input of highly subjective assumptions, including the expected life of the stock-based payment awards and stock price volatility. Management estimates the volatility based on the historical volatility of our stock. The assumptions used in calculating the fair value of stock-based payment awards represent management's best estimates, but these estimates involve inherent uncertainties and the application of management's judgment. As a result, if circumstances change and we use different assumptions, our stock-based compensation expense could be materially different in the future. In addition, we are required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. If our actual forfeiture rate is materially different from our estimate, the stock-based compensation expense could be significantly different from what it has recorded in the current period. The estimated fair value of our stock-based options and performance-based restricted stock units (RSUs), less expected forfeitures, is amortized over the awards' vesting period on a graded vesting basis, whereas the RSUs and employee stock purchase plan stock units are amortized on a straight-line basis.

Advertising Costs

Advertising costs are charged to expense as incurred. Advertising costs were \$0.1 million, \$0.1 million and \$0.2 million for fiscal 2015, 2014 and 2013, respectively.

Earnings Per Share

Earnings per share are presented in accordance with authoritative guidance which requires the presentation of basic earnings per share and diluted earnings per share. Basic earnings per share is computed by dividing

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earnings available to common shareholders by the weighted-average shares of common stock outstanding during the period. For the purposes of calculating diluted earnings per share, the denominator includes both the weighted average number of shares of common stock outstanding during the period and the weighted average number of potential shares of common stock, such as stock options and restricted stock, calculated using the treasury stock method. For the purpose of calculating diluted loss per share, we do not include these shares in the denominator because these shares would have an anti-dilutive effect on periods in which we incur a net loss. Certain shares of our common stock have exercise prices in excess of the average market price. These shares are anti-dilutive and are omitted from the calculation of earnings per share. For more information on this see Note 14., *Net Loss Per Share*, below.

Recent Accounting Pronouncements

We consider the applicability and impact of all Accounting Standards Updates. Updates not listed below were assessed and determined to be either not applicable or are expected to have minimal impact on our consolidated financial position or results of operations.

Recent Accounting Guidance Not Yet Effective***Amendments to the Consolidation Analysis***

In February 2015, the FASB issued ASU 2015-02, *Amendments to the Consolidation Analysis*. ASU 2015-02 is intended to improve guidance for limited partnerships, limited liability corporations and securitization structures. The guidance places more emphasis on risk of loss when determining a controlling financial interest, reduces the frequency of the application of related-party guidance when determining a controlling financial interest in a VIE and changes consolidation conclusions for public and private companies that typically make use of limited partnerships or VIEs. This guidance is effective for us beginning in fiscal 2017. Early adoption is permitted. We are currently evaluating the impact of the adoption of ASU 2015-02 on our consolidated financial statements.

Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Item

In January 2015, the FASB issued ASU 2015-01, *Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Item*. ASU 2015-01 is meant to reduce complexity in accounting standards by eliminating the concept of extraordinary items from U.S. GAAP. In the event of a transaction that meets the criteria for extraordinary classification, an entity is required to segregate the extraordinary item from the results of ordinary operations and show the item separately in the income statement, net of tax after income from continuing operations. This new guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. A reporting entity may apply the amendments prospectively. A reporting entity also may apply the amendments retrospectively to all prior periods presented in the financial statements. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. Besides presentation on the consolidated statements of operations and comprehensive (loss) income when an item that meets the extraordinary criteria exists, we do not feel that adoption of ASU 2015-01 will have a material impact on our consolidated financial statements.

Accounting For Share-Based Payments Performance Target Could Be Achieved after the Requisite Service Period

In June 2014, the FASB issued ASU 2014-12, *Compensation Stock Compensation (Topic 718) Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period*. ASU 2014-12 requires that a performance target which affects vesting and that could be achieved after the requisite service period be treated as a performance condition by applying existing guidance in

Topic 718 as it relates to awards with performance conditions. The amendment also specifies the period over which compensation costs should be recognized. The amendment is effective for annual

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reporting periods and interim periods within those annual periods beginning after December 15, 2015. Early adoption is permitted. We are currently evaluating the impact of the adoption of ASU 2014-12 on our consolidated financial statements.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and the International Financial Reporting Standards. This guidance supersedes previously issued guidance on revenue recognition and gives a five step process an entity should follow so that the entity recognizes revenue that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This new guidance will be effective for our fiscal 2018 reporting period and must be applied either retrospectively during each prior reporting period presented or retrospectively with the cumulative effect of initially applying this guidance recognized at the date of the initial application. Early adoption is not permitted. We are currently evaluating the impact of the adoption of this ASU on our consolidated financial statements.

Reporting Discontinued Operations and Disposals of Components of an Entity

In April 2014, the FASB issued ASU 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360) Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*, which changes the criteria for reporting discontinued operations while enhancing disclosures in this area. The amended guidance requires that a disposal representing a strategic shift that has (or will have) a major effect on an entity's financial results or a business activity classified as held for sale should be reported as discontinued operations. This guidance also expands the disclosures required when an entity reports a discontinued operation or when it disposes of or classifies as held for sale an individually significant component that does not meet the definition of a discontinued operation. This new guidance will be effective prospectively on disposals (or classifications of held for sale) of components of an entity that occur within our fiscal year beginning on February 1, 2015. Early adoption is permitted but only for disposals (or classification as held for sale) that have not been reported in financial statements previously issued or available for issuance. We do not anticipate material impacts on our financial statements upon initial adoption. This guidance could have a material impact on our disclosure requirements if we dispose of, or classify as held for sale, an individually significant component of our business that does not meet the definition of a discontinued operation.

3. Discontinued Operations

On May 4, 2012, we completed the sale of our broadcast servers and storage business and received a cash payment, net of certain adjustments, of \$4.9 million and recorded a total gain in this transaction, net of tax in the amount of \$1.5 million. The financial results from this divested business are included in discontinued operations in our consolidated statements of operations and comprehensive loss.

On May 21, 2012, we completed the sale of our media services business, ODG, to Avail Media, Inc. (Avail) for a purchase price of approximately \$27 million plus certain working capital adjustments. We recorded a \$15.5 million loss in our consolidated statements of operations and comprehensive loss from the sale of ODG, primarily arising from a related \$17.0 million goodwill impairment charge that we recorded in the first quarter of fiscal 2013. The financial results from our former media services segment are included as discontinued operations in our consolidated statements of operations and comprehensive loss.

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The following table details selected financial information for our former broadcast servers and storage and media services business units for the periods presented (amounts in thousands):

	For the Fiscal Year Ended January 31, 2014			For the Fiscal Year Ended January 31, 2013		
	Servers and Storage	Media Services	Total Discontinued Operations	Servers and Storage	Media Services	Total Discontinued Operations
Revenues:						
Products	\$ 46	\$	\$ 46	\$ 1,031	\$	\$ 1,031
Services				835	9,315	10,150
Total revenues	\$ 46	\$	\$ 46	\$ 1,866	\$ 9,315	\$ 11,181
Income (loss) from discontinued operations:						
Loss from discontinued operations, before tax	\$ (803)	\$	\$ (803)	\$ (1,854)	\$ (194)	\$ (2,048)
Income tax provision (benefit)				84	(13)	71
Income in investment in affiliates					(174)	(174)
Loss from discontinued operations, after tax	\$ (803)	\$	\$ (803)	\$ (1,938)	\$ (355)	\$ (2,293)

4. Fair Value Measurements*Fair Value Measurements of Assets and Liabilities*

The following tables set forth our financial assets and liabilities that were accounted for at fair value on a recurring basis as of January 31, 2015 and January 31, 2014:

	Fair Value at January 31, 2015 Using		
	Quoted Prices in Active Markets for Identical Assets January 31, 2015	Significant Other Observable Inputs (Level 2) (Amounts in thousands)	Significant Unobservable Inputs (Level 3)
Financial assets:			
Money market accounts (a)	\$ 1,575	\$ 1,575	\$
Available for sale marketable securities:			

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Current marketable securities:

U.S. treasury notes and bonds conventional	1,501	1,501		
U.S. government agency issues	6,015		6,015	

Non-current marketable securities:

U.S. treasury notes and bonds conventional	4,286	4,286		
U.S. government agency issues	2,507		2,507	

Total	\$ 15,884	\$ 7,362	\$ 8,522	\$
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	Fair Value at January 31, 2014 Using Quoted Prices in Active Markets for Identical Assets January 31, 2014			
	(Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
	(Amounts in thousands)			
Financial assets:				
Money market accounts (a)	\$ 3,463	\$ 3,463	\$	\$
Available for sale marketable securities:				
Current marketable securities:				
U.S. treasury notes and bonds conventional	3,545	3,545		
U.S. government agency issues	2,010	2,010		
Non-current marketable securities:				
U.S. government agency issues	6,814	6,814		
Total	\$ 15,832	\$ 7,008	\$ 8,824	\$

- a) Money market funds and U.S. treasury bills are included in cash and cash equivalents on the accompanying consolidated balance sheet and are valued at quoted market prices for identical instruments in active markets.

Available-for-Sale Securities

We determine the appropriate classification of debt securities at the time of purchase and reevaluate such designation as of each balance sheet date. Our investment portfolio consists of money market funds, U.S. treasury notes and bonds, and U.S. government agency notes and bonds as of January 31, 2015 and 2014. All highly liquid investments with an original maturity of three months or less when purchased are considered to be cash equivalents. All cash equivalents are carried at cost, which approximates fair value. Our marketable securities are classified as available-for-sale and are reported at fair value with unrealized gains and losses, net of tax, reported in stockholders equity as a component of accumulated other comprehensive loss. The amortization of premiums and accretion of discounts to maturity are computed under the effective interest method and is included in other expenses, net. Interest on securities is recorded as earned and is also included in other expenses, net. Any realized gains or losses would be shown in the accompanying consolidated statements of operations and comprehensive loss in other expenses, net.

The following is a summary of cash, cash equivalents and available-for-sale securities, including the cost basis, aggregate fair value and unrealized gains and losses, for short-and long-term marketable securities portfolio as of January 31, 2015 and 2014:

Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(Amounts in thousands)			

January 31, 2015:

Cash	\$ 88,444	\$	\$	\$ 88,444
Cash equivalents	1,575			1,575
Cash and cash equivalents	90,019			90,019
U.S. treasury notes and bonds short-term	1,500	1		1,501
U.S. treasury notes and bonds long-term	4,268	18		4,286
U.S. government agency issues short-term	6,008	7		6,015
U.S. government agency issues long-term	2,490	17		2,507
Total cash, cash equivalents and marketable securities	\$ 104,285	\$ 43	\$	\$ 104,328

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	Amortized Cost	Gross Unrealized Gains (Amounts in thousands)	Gross Unrealized Losses	Estimated Fair Value
January 31, 2014:				
Cash	\$ 112,271	\$	\$	\$ 112,271
Cash equivalents	3,463			3,463
Cash and cash equivalents	115,734			115,734
U.S. treasury notes and bonds short-term	3,540	5		3,545
U.S. government agency issues short-term	2,005	5		2,010
U.S. government agency issues long-term	6,806	8		6,814
Total cash, cash equivalents and marketable securities	\$ 128,085	\$ 18	\$	\$ 128,103

The gross realized gains and losses on sale of available-for-sale securities for fiscal years 2015, 2014 and 2013 were immaterial. For purposes of determining gross realized gains and losses, the cost of securities sold is based on specific identification.

Contractual maturities of available-for-sale debt securities at January 31, 2015 are as follows (amounts in thousands):

	Estimated Fair Value
Maturity of one year or less	\$ 7,516
Maturity between one and five years	6,793
Total	\$ 14,309

We concluded that there were no other than temporary declines in investments recorded as of January 31, 2015, 2014 and 2013. The unrealized holding gains (losses), net of tax, on available-for-sale securities, which are not material for the periods presented, have been included in stockholders' equity as a component of accumulated other comprehensive loss.

Cash, Cash Equivalents and Marketable Securities

Cash and cash equivalents consist primarily of highly liquid investments in money market mutual funds, government sponsored enterprise obligations, treasury bills, commercial paper and other money market securities with remaining maturities at date of purchase of 90 days or less.

Restricted Cash

In December 2014, in conjunction with our acquisition of TLL, LLC (Timeline Labs), we entered into an agreement to fund a \$2.5 million escrow from which Timeline Labs could make withdrawals for working capital purposes. The withdrawn portion of the escrow is accounted for as an advance against the purchase price and is recorded in other

assets on our consolidated balance sheets. The unused portion, being \$1.1 million remaining in escrow after signing the related merger agreement but prior to the consummation of the acquisition on February 2, 2015, is classified as restricted cash on our consolidated balance sheets. See Note 16., *Subsequent Events*, for additional information.

The fair value of cash, cash equivalents, restricted cash and marketable securities at January 31, 2015 and 2014 was \$105.4 million and \$128.1 million, respectively.

Table of Contents**5. Consolidated Balance Sheet Detail**

Inventories consist primarily of hardware and related component parts and are stated at the lower of cost (on a first-in, first-out basis) or market. Inventories consist of the following:

	January 31,	
	2015	2014
	(Amounts in thousands)	
Components and assemblies	\$ 1,487	\$ 2,201
Finished products	1,377	4,431
Total inventories	\$ 2,864	\$ 6,632

Property and equipment, net consists of the following:

	Estimated Useful Life (Years)	January 31,	
		2015	2014
		(Amounts in thousands)	
Land		\$ 2,880	\$ 2,880
Buildings	20	12,146	12,081
Office furniture and equipment	5	1,023	998
Computer equipment, software and demonstration equipment	3	17,584	17,466
Service and spare components	5	1,158	1,158
Leasehold improvements	1-7	1,089	1,145
		35,880	35,728
Less Accumulated depreciation and amortization		(20,011)	(17,198)
Total property and equipment, net		\$ 15,869	\$ 18,530

Depreciation and amortization expense of fixed assets was \$3.7 million, \$4.4 million and \$4.7 million for the years ended January 31, 2015, 2014 and 2013, respectively.

Other accrued expenses consist of the following:

	January 31,	
	2015	2014
	(Amounts in thousands)	
Accrued compensation and commissions	\$ 1,518	\$ 2,290

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Accrued bonuses	2,186	2,095
Accrued severance	2,021	229
Employee benefits	1,959	2,113
Accrued other	4,823	5,605
Total other accrued expenses	\$ 12,507	\$ 12,332

6. Goodwill and Intangible Assets

At January 31, 2015 and 2014, we had goodwill of \$41.0 million and \$45.2 million, respectively. The change in the carrying amount of goodwill for the years ended January 31, 2015 and 2014 are as follows (amounts in thousands):

	Goodwill
Balance at January 31, 2013	\$ 45,103
Cumulative translation adjustment	47
Balance at January 31, 2014	45,150
Cumulative translation adjustment	(4,142)
Balance at January 31, 2015	\$ 41,008

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We are required to perform impairment tests related to our goodwill annually, which we perform during the third quarter of each fiscal year, or when an indicator of impairment occurs. There was no impairment of goodwill determined as a result of the annual impairment test completed during the third quarter of fiscal 2015. While no impairment charges resulted from our annual test, impairment charges may occur in the future as a result of changes in projected growth and other factors.

Intangible assets, net, consisted of the following at January 31, 2015 and 2014:

	Weighted average remaining life (Years)	January 31, 2015			January 31, 2014		
		Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Finite-lived intangible assets:							
Customer contracts	6.0	\$ 30,397	\$ (24,160)	\$ 6,237	\$ 32,593	\$ (22,344)	\$ 10,249
Non-compete agreements		2,433	(2,433)		2,772	(2,632)	140
Completed technology	5.2	10,307	(9,230)	1,077	11,461	(9,195)	2,266
Trademarks, patents and other		7,082	(7,082)		7,151	(7,151)	
Total finite-lived intangible assets		\$ 50,219	\$ (42,905)	\$ 7,314	\$ 53,977	\$ (41,322)	\$ 12,655
Indefinite-lived intangible assets:							
Trade names					200		200
Total intangible assets		\$ 50,219	\$ (42,905)	\$ 7,314	\$ 54,177	\$ (41,322)	\$ 12,855

Amortization expense for intangible assets was \$5.2 million, \$4.6 million and \$6.4 million for fiscal 2015, 2014 and 2013, respectively.

The total amortization expense for each of the next five fiscal years is as follows (amounts in thousands):

For the Fiscal Years Ended January 31,	Estimated Amortization Expense
2016	\$ 3,076
2017	2,195
2018	1,272
2019	649
2020	121
Fiscal 2021 and thereafter	1

Total Future Amortization	\$	7,314
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Actual amortization may differ from estimated amounts in the table above due to fluctuations in foreign currency exchange rates, additional intangible asset acquisitions, potential impairment, accelerated amortization, or other events. During fiscal 2015, we fully amortized our trade name intangible assets as they are no longer in use.

7. Severance and Other Restructuring Costs

During fiscal 2015, we incurred restructuring charges totaling \$3.6 million. These charges included \$3.4 million of severance costs for terminated employees. In addition, we incurred \$0.2 million of other restructuring charges primarily due to the write off of leasehold improvements.

As announced in February 2015, we initiated a global restructuring plan to streamline our operations. The reduction in our domestic work force was implemented in January 2015 and estimated charges were recorded. We will implement an international reduction in workforce in fiscal 2016 and expect to incur future restructuring charges.

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The following table shows the change in balances of our accrued severance reported as a component of other accrued expenses on the consolidated balance sheets (amounts in thousands):

Accrual balance as of January 31, 2014	\$ 229
Restructuring charges incurred	3,623
Severance costs paid	(1,605)
Other charges	(226)
Accrual balance as of January 31, 2015	\$ 2,021

8. Commitments and Contingencies***Indemnification and Warranties***

We provide indemnification, to the extent permitted by law, to our officers, directors, employees and agents for liabilities arising from certain events or occurrences while the officer, director, employee or agent is, or was, serving at our request in such capacity. With respect to acquisitions, we provide indemnification to, or assume indemnification obligations for, the current and former directors, officers and employees of the acquired companies in accordance with the acquired companies' bylaws and charters. As a matter of practice, we have maintained directors' and officers' liability insurance including coverage for directors and officers of acquired companies.

We enter into agreements in the ordinary course of business with customers, resellers, distributors, integrators and suppliers. Most of these agreements require us to defend and/or indemnify the other party against intellectual property infringement claims brought by a third party with respect to our products. From time to time, we also indemnify customers and business partners for damages, losses and liabilities they may suffer or incur relating to personal injury, personal property damage, product liability, and environmental claims relating to the use of our products and services or resulting from the acts or omissions of us, our employees, authorized agents or subcontractors. From time to time, we have received requests from customers for indemnification of patent litigation claims. Management cannot reasonably estimate any potential losses, but these claims could result in material liability for us. We are not party to current pending legal proceedings that, in the opinion of management, would have a material adverse effect on our financial position, results from operations and cash flows. There is no assurance that future legal proceedings arising from ordinary course of business or otherwise, will not have a material adverse effect on our financial position, results from operations or cash flows.

We warrant that our products, including software products, will substantially perform in accordance with our standard published specifications in effect at the time of delivery. In addition, we provide maintenance support to our customers and therefore allocate a portion of the product purchase price to the initial warranty period and recognize revenue on a straight line basis over that warranty period related to both the warranty obligation and the maintenance support agreement. When we receive revenue for extended warranties beyond the standard duration, it is deferred and recognized on a straight line basis over the contract period. Related costs are expensed as incurred.

Revolving Line of Credit/Demand Note Payable

We renewed our letter agreement for a demand discretionary line of credit and a Demand Promissory Note in the aggregate amount of \$20.0 million, effective November 26, 2014. Borrowings under the line of credit will be used to finance working capital needs and for general corporate purposes. We currently do not have any borrowings nor do we

have any financial covenants under this line.

Table of Contents***Operating Leases***

We lease certain of our operating facilities, automobiles and office equipment under non-cancelable operating leases, which expire at various dates through 2019. Leases for our facilities typically contain standard commercial lease provisions, including renewal options and rent escalation clauses. Rental expense under operating leases was \$2.9 million, \$2.4 million and \$2.7 million for fiscal 2015, 2014 and 2013, respectively. Future commitments under minimum lease payments as of January 31, 2015 are as follows (amounts in thousands):

For the Fiscal Years Ended January 31,	Operating Leases
2016	\$ 2,261
2017	1,680
2018	477
2019	30
2020	
2021 and thereafter	
Minimum operating lease payments	\$ 4,448

9. Stockholders Equity***Stock Authorization***

The Board of Directors is authorized to issue from time to time up to an aggregate of 5,000,000 shares of preferred stock, in one or more series. Each such series of preferred stock shall have the number of shares, designations, preferences, voting powers, qualifications and special or relative rights or privileges to be determined by the Board of Directors, including dividend rights, voting rights, redemption rights and sinking fund provisions, liquidation preferences, conversion rights and preemptive rights. No preferred stock has been issued as of January 31, 2015.

Stock Repurchase Program

On September 4, 2013, our Board of Directors authorized the repurchase of up to \$25.0 million of our common stock through a share repurchase program which would have terminated on January 31, 2015. On May 31, 2014, this program was amended to increase the authorized repurchase amount to \$40.0 million and extend the termination date to April 30, 2015. Under the program, we are authorized to repurchase shares through Rule 10b5-1 plans, open market purchases, privately negotiated transactions, block purchases or otherwise in accordance with applicable federal securities laws, including Rule 10b-18 of the Securities Exchange Act of 1934. This share repurchase program does not obligate us to acquire any specific number of shares and may be suspended or discontinued at any time. All repurchases are expected to be funded from our current cash and investment balances. The timing and amount of shares to be repurchased will be based on market conditions and other factors, including price, corporate and regulatory requirements, and alternative investment opportunities. Any shares repurchased by us under the share repurchase program will reduce the number of shares outstanding. Pursuant to the share repurchase program, we executed a Rule 10b5-1 plan in June 2014 to repurchase shares. During fiscal 2015, we used \$5.5 million of cash in connection with the repurchase of 591,520 shares of our common stock (an average price of \$9.31 per share). As of January 31, 2015, \$34.5 million remained available to repurchase under the existing share repurchase authorization.

Stock Option Plans

2011 Compensation and Incentive Plan.

In July 2011, our stockholders approved the adoption of our 2011 Compensation and Incentive Plan (the 2011 Plan). Under the 2011 Plan, as amended in July 2013, the number of authorized shares of common stock is

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equal to 5,300,000 shares plus the number of shares that would have become available for issuance under our prior Amended and Restated 2005 Equity Compensation and Incentive Plan following the adoption of the 2011 Plan due to the expiration, termination, surrender or forfeiture of an award under the prior plan. The 2011 Plan provides for the grant of incentive stock options, nonqualified stock options, restricted stock, RSUs, deferred stock units (DSUs) and other equity based non-stock option awards as determined by the plan administrator, to officers, employees, consultants, and directors of the Company.

Effective February 1, 2014, SeaChange gave its non-employee members of the Board of Directors the option to receive DSUs in lieu of RSUs beginning with the annual grant for fiscal 2015. These DSUs shall fully vest one year from the grant date. The number of units subject to the DSUs is determined as of the first day of the applicable fiscal year and the shares underlying the DSUs are not vested and issued until the earlier of the director ceasing to be a member of the Board of Directors (provided such time is subsequent to the first day of the succeeding fiscal year) or immediately prior to a change in control.

We may satisfy awards upon the exercise of stock options or vesting of RSUs with newly issued shares or treasury shares. The Board of Directors is responsible for the administration of the 2011 Plan and determining the terms of each award, award exercise price, the number of shares for which each award is granted and the rate at which each award vests. In certain instances the Board of Directors may elect to modify the terms of an award. As of January 31, 2015, there were 2,484,004 shares available for future grant under the 2011 Plan.

Option awards may be granted to employees at an exercise price per share of not less than 100% of the fair market value per common share on the date of the grant. RSUs, DSUs and other equity-based non-stock option awards may be granted to any officer, employee, director, or consultant at a purchase price per share as determined by the Board of Directors. Option awards granted under the 2011 Plan generally vest over a period of three years and expire ten years from the date of the grant.

Stock-based Compensation

We use the provisions of the authoritative guidance which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors including employee stock options, RSUs and DSUs based on estimated fair values. The fair value of our stock-based options and performance-based RSUs, less expected forfeitures, is amortized over the awards' vesting period on a graded vesting basis, whereas the RSUs are amortized on a straight-line basis. We have applied the provisions of authoritative guidance allowing the use of a simplified method, in developing an estimate of the expected term of plain vanilla share options.

Stock-based compensation includes expense charges for all stock-based awards to employees and directors. Such awards include option grants, RSU and DSU awards. The estimated fair value of our stock-based options and performance-based RSUs, less expected forfeitures, is amortized over the awards' vesting period on a graded vesting basis, whereas the RSUs and DSUs are amortized on a straight-line basis.

The effect of recording stock-based compensation was as follows:

For the Fiscal Years Ended January 31,		
2015	2014	2013
(Amounts in thousands)		

Stock-based compensation expense by type of award:			
Stock options	\$ 1,036	\$ 453	\$ 3,586
Restricted stock units	1,607	1,907	2,218
Deferred stock units	500		
Performance-based restricted stock units	77	599	125
Total stock-based compensation	\$ 3,220	\$ 2,959	\$ 5,929

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Since additional option grants and RSU awards are expected to be made each year and options and awards vest over several years, the effects of applying authoritative guidance for recording stock-based compensation for the year ended January 31, 2015 are not indicative of future amounts.

Determining Fair Value***Stock Options***

We record the fair value of most stock options using the Black-Scholes valuation model. Key input assumptions used to estimate the fair value of stock options include the exercise price, the expected option term, the risk-free interest rate over the option's expected term, the expected annual dividend yield and the expected stock price volatility. The expected option term was determined using the simplified method for plain vanilla options. The expected stock price volatility was established using a blended volatility, which is an average of the historical volatility of our common stock over a period of time equal to the expected term of the stock option, and the average volatility of our common stock over the most recent one-year and two-year periods. The risk-free interest rate is based upon the U.S. treasury bond yield at the grant date, using a remaining term equal to the expected life. The expected dividend yield is 0%, as we have not paid cash dividends on our common stock since our inception.

The fair value of stock options granted was estimated at the date of grant using the following assumptions:

	For the Fiscal Years Ended January 31,		
	2015	2014	2013
Expected term (in years)	6.5	5-7	3-7
Expected volatility (range)	46%	44-46%	49-52%
Weighted average volatility	46%	45%	52%
Risk-free interest rate	1.7%	0.7-0.9%	0.7-1.2%
Weighted average interest rate	1.7%	0.8%	1.2%
Expected dividend yield	0%	0%	0%

Market-Based Options

When market-based vesting is used on stock options (Market Condition Options) we use the Monte Carlo simulation model. The model simulates daily trading prices of the Market Condition Options' expected term to determine if vesting conditions would be triggered during that term.

We appointed a new CEO on October 20, 2014, at which time he was granted 500,000 stock options to purchase the Company's common stock. These stock options have an exercise price equal to our closing stock price on October 20, 2014, and will vest in approximately equal increments based upon the closing price of our common stock, but in no case earlier than six months from the date of grant. We recorded the fair value of these stock options using the Monte Carlo simulation model, since the stock option vesting is variable depending on the closing price of our traded common stock. Key input assumptions used to estimate the fair value of the Market Condition Options include exercise price, volatility, risk-free rate, the required rate of return on equity, annual turnover rate and the expected term to exercise. These assumptions are included in the table above for fiscal 2015. No other options were granted during this fiscal year. The model simulated the daily trading price of the Market Condition Options' expected term to determine if the vesting conditions would be triggered during the term. As a result, the fair value of these stock options was estimated at \$1.7 million. We have incurred stock compensation expense of \$0.3 million for the period from the date of grant to and including January 31, 2015.

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The following table summarizes the stock option activity (excluding RSUs and DSUs):

	For the Fiscal Years Ended January 31,					
	2015		2014		2013	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Outstanding at beginning of period	1,502,176	\$ 9.77	1,917,448	\$ 10.35	2,125,371	\$ 11.83
Granted	500,000	\$ 7.23	12,500	\$ 10.10	892,500	\$ 8.21
Exercised		\$	(118,528)	\$ 9.10	(304,550)	\$ 7.19
Forfeited/expired/cancelled	(375,755)	\$ 15.06	(309,244)	\$ 13.78	(795,873)	\$ 13.11
Outstanding at end of period	1,626,421	\$ 7.77	1,502,176	\$ 9.77	1,917,448	\$ 10.35
Options exercisable at end of period	1,108,115	\$ 8.02	1,440,521	\$ 9.90	937,444	\$ 12.78
Weighted average remaining contractual term (in years)		4.72		3.93		1.86

The weighted-average fair valuation at grant date of stock options granted during the years ended January 31, 2015, 2014 and 2013, was \$3.39, \$1.53, and \$3.78, respectively. As of January 31, 2015, the unrecognized stock-based compensation related to the unvested stock options was approximately \$1.4 million, net of estimated forfeitures. Total unrecognized compensation cost will be adjusted for any future changes in estimated changes in forfeitures. This cost will be recognized over an estimated weighted average amortization period of 1.6 years.

Intrinsic value is defined as the difference between the market price on the date of exercise and the grant date price. The aggregate intrinsic value for options outstanding was \$0.1 million, \$4.5 million and \$1.4 million as of January 31, 2015, 2014 and 2013, respectively. The aggregate intrinsic value of vested shares and share options expected to vest as of January 31, 2015, 2014 and 2013 was \$0.1 million, \$4.4 million and \$1.3 million, respectively. There were no stock options exercised in fiscal 2015. The total intrinsic value of options exercised during the years ended January 31, 2014 and 2013 was \$0.3 million and \$0.5 million, respectively.

The cash received from employees as a result of employee stock option exercises during fiscal years 2014 and 2013 was \$1.1 million and \$2.2 million, respectively.

The following table summarizes information about employee and director stock options outstanding and exercisable as of January 31, 2015:

Options Outstanding			Options Exercisable	
Number outstanding	Weighted average remaining contractual terms	Weighted average exercise price	Number exercisable	Weighted average exercise price

(years)

Range of exercise prices					
\$6.74 to \$6.74	224,421	3.96	\$ 6.74	207,781	\$ 6.74
\$7.00 to \$7.48	501,000	6.10	\$ 7.23	1,000	\$ 7.00
\$7.49 to \$7.49	1,000	0.35	\$ 7.49	1,000	\$ 7.49
\$7.72 to \$7.72	4,500	0.44	\$ 7.72	4,500	\$ 7.72
\$8.15 to \$8.15	5,000	4.42	\$ 8.15	3,334	\$ 8.15
\$8.22 to \$8.22	875,000	4.24	\$ 8.22	875,000	\$ 8.22
\$11.56 to \$11.56	2,000	0.19	\$ 11.56	2,000	\$ 11.56
\$12.95 to \$12.95	2,000	0.17	\$ 12.95	2,000	\$ 12.95
\$13.66 to \$13.66	6,500	0.09	\$ 13.66	6,500	\$ 13.66
\$16.56 to \$16.56	5,000	0.01	\$ 16.56	5,000	\$ 16.56
	1,626,421	4.72	\$ 7.77	1,108,115	\$ 8.02

Table of Contents**Restricted Stock Units and Deferred Stock Units**

Pursuant to the 2011 Plan, we may grant RSUs and DSUs that entitle the recipient to acquire shares of our common stock. Awards of RSUs generally vest in equal increments on each of the first three anniversaries of the grant of the award. DSUs generally vest on the first anniversary of the grant. Stock-based compensation expense associated with the RSUs and DSUs is charged for the market value of our stock on the date of grant, assuming nominal forfeitures, and is amortized over the awards' vesting period on a straight-line basis for awards with only a service condition and graded vesting basis for awards that include both a performance and service condition.

The following table summarizes the RSU and DSU activity:

	For the Fiscal Years Ended January 31,					
	2015		2014		2013	
	Shares	Weighted average grant date fair value	Shares	Weighted average grant date fair value	Shares	Weighted average grant date fair value
Nonvested at beginning of period	446,468	\$ 9.81	552,980	\$ 10.51	721,365	\$ 10.46
Awarded	314,057	\$ 8.60	146,411	\$ 11.15	375,317	\$ 8.62
Vested	(287,485)	\$ 9.83	(205,928)	\$ 12.61	(348,346)	\$ 8.73
Forfeited/expired/cancelled	(37,734)	\$ 10.01	(46,995)	\$ 9.93	(195,356)	\$ 9.87
Nonvested at end of period	435,306	\$ 8.91	446,468	\$ 9.81	552,980	\$ 10.51

As of January 31, 2015, the unrecognized stock-based compensation related to the unvested RSUs and DSUs was \$2.2 million. This cost will be recognized over an estimated weighted average amortization period of 2.3 years.

10. Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss consisted of the following:

	Changes in Foreign Fair Value of Accumulated Currency Available for Translation for-Sale Investments		
	Adjustments	Investments	Loss
Balance at January 31, 2013	\$ (1,856)	\$ 30	\$ (1,826)
Other comprehensive loss	(294)	(12)	(306)

Balance at January 31, 2014							
December 31, 2010	Past Due and Still	Past Due and Still	Past Due and Still	And Still	Current	Nonaccrual	Total
(In Thousands)	Accruing	Accruing	Accruing	Accruing	Balances	Loans	Loans
Commercial	\$2,839	\$384	\$-	\$3,223	\$1,213,246	\$21,577	\$1,238,046
Commercial mortgages	764	-	-	764	611,744	9,490	621,998
Construction	1,685	-	-	1,685	108,714	30,260	140,659
Residential	6,403	2,024	465	8,892	289,864	11,739	310,495
Consumer	1,355	163	-	1,518	305,290	3,701	310,509
Total	\$13,046	\$2,571	\$465	\$16,082	\$2,528,858	\$76,767	\$2,621,707
% of Total Loans	0.49 %	0.10 %	0.02 %	0.61 %	96.46 %	2.93 %	100 %

Impaired Loans

The following tables provide an analysis of our impaired loans at September 30, 2011 and December 31, 2010:

	Ending	Loans with No	Loans with	Related	Contractual	Average
September 30, 2011	Loan	Specific Reserve	Specific Reserve	Specific Reserve	Principal Balances	Loan Balances
(In Thousands)	Balances	(1)	Reserve	Reserve	Balances	Balances
Commercial	\$ 21,270	\$ 18,381	\$ 2,889	\$ 1,810	\$ 30,291	\$ 22,196
Commercial mortgages	20,306	11,960	8,346	1,604	28,728	16,251
Construction	21,701	3,687	18,014	3,005	44,010	28,622
Residential	17,666	11,419	6,247	808	20,740	17,794
Consumer	3,176	1,880	1,296	120	3,728	4,240
Total	\$ 84,119	\$ 47,327	\$ 36,792	\$ 7,347	\$ 127,497	\$ 89,103

	Ending	Loans with No Specific Reserve (1)	Loans with Specific Reserve	Related Specific Reserve	Contractual Principal Balances	Average Loan Balances
December 31, 2010	Loan					
(In Thousands)	Balances					
Commercial	\$ 21,527	\$ 14,555	\$ 6,972	\$ 4,845	\$ 29,309	\$ 16,139
Commercial mortgages	9,490	3,263	6,227	2,591	12,001	4,530
Construction	30,260	12,166	18,094	3,485	53,265	36,102
Residential	17,441	11,226	6,215	968	22,112	16,667
Consumer	5,106	3,969	1,137	130	6,558	4,184
Total	\$ 83,824	\$ 45,179	\$ 38,645	\$ 12,019	\$ 123,245	\$ 77,622

(1) Reflects loan balances at their remaining book balance.

Interest income of \$94,000 and \$279,000 was recognized on impaired loans during the three and nine months ended September 30, 2011, respectively.

Credit Quality Indicators

Below is a description of each of our risk ratings for all commercial loans:

Pass. These assets presently show no current or potential problems and are considered fully collectible.

Special Mention. These assets do not currently expose the Bank to a sufficient degree of risk to warrant an adverse classification but do possess credit deficiencies or potential weaknesses deserving our close attention. Special mention assets have a potential weakness or pose an unwarranted financial risk which, if not corrected, could weaken the asset and increase risk in the future.

Substandard. Assets which are inadequately protected by the current net worth and paying capacity of the obligor or collateral, if any. Assets so classified have a well-defined weakness or weaknesses based upon objective evidence that jeopardizes the timely liquidation of the asset, or realization of the collateral at the asset's net book value. Substandard assets can be classified as accrual or nonaccrual and are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. The possibility of untimely liquidation requires a substandard classification even if there is little likelihood of total loss.

Doubtful. The rating designated to assets with all the weaknesses of substandard assets and added weaknesses that make collection in full highly questionable and improbable, on the basis of currently existing facts, conditions, and values.

Loss. These assets are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that an asset has absolutely no recovery or salvage value, but rather, that it is not practical or desirable to defer writing off a mostly worthless asset even though partial recovery may occur in the future.

Residential and Consumer Loans

The residential and consumer loan portfolios are monitored on an ongoing basis using delinquency information and loan type as credit quality indicators. These credit quality indicators are assessed in the aggregate in these relatively homogeneous portfolios. Loans that are greater than 90 days past due are generally considered nonperforming and placed in nonaccrual status.

The following tables provide an analysis of problem loans as of September 30, 2011 and December 31, 2010:

Commercial credit exposure credit risk profile by internally assigned risk rating (in thousands):

	Commercial		Commercial Mortgages		Construction		Total Commercial		December 31, 2010	
	Sept. 30, 2011	Dec. 31, 2010	Sept. 30, 2011	Dec. 31, 2010	Sept. 30, 2011	Dec. 31, 2010	September 30, 2011 Amount	Percent	Amount	Percent
Risk Rating:										
Special mention	\$74,727	\$39,544	\$30,514	\$13,195	\$11,328	\$21,970	\$116,569		\$74,709	
Substandard:										
Accrual	67,197	54,230	4,291	21,121	17,988	32,560	89,476		107,911	
Nonaccrual	21,370	21,577	20,875	9,490	21,701	30,260	63,946		61,327	
Total Special Mention and Substandard	163,294	115,351	55,680	43,806	51,017	84,790	269,991	13%	243,947	100%
Pass	1,234,248	1,122,695	548,190	578,192	60,487	55,869	1,842,925	87%	1,756,756	87%
Total Commercial Loans	\$1,397,542	\$1,238,046	\$603,870	\$621,998	\$111,504	\$140,659	\$2,112,916	100%	\$2,000,703	100%

Consumer credit exposure credit risk profile based on payment activity (in thousands):

	Residential		Consumer		Total Residential and Consumer			
	Sept. 30, 2011	Dec.31, 2010	Sept. 30, 2011	Dec.31, 2010	September 30, 2011 Amount	Percent	December 31, 2010 Amount	Percent
Nonperforming	\$ 17,666 (1)	\$ 17,441	\$ 3,176 (1)	\$ 5,106	\$ 20,842	4 %	\$ 22,547	4 %
Performing	267,668	293,054	293,991	305,403	561,659	96	598,457	96
Total	\$ 285,334	\$ 310,495	\$ 297,167	\$ 310,509	\$ 582,501	100 %	\$ 621,004	100 %

(1) Includes \$8.7 million of troubled debt restructured mortgages and home equity installment loans performing in accordance with modified terms and are accruing interest.

Troubled Debt Restructurings (TDR)

Effective July 1, 2011, we adopted the provisions of Accounting Standards Update No. 2011-02, A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring. As such, we reassessed all loan modifications occurring since January 1, 2011 for identification as TDRs, resulting in no newly identified TDRs.

The book balance of TDRs at September 30, 2011 and December 31, 2010 was \$27.7 million and \$12.0 million, respectively. The balances at September 30, 2011 include approximately \$19.0 million of TDRs in nonaccrual status and \$8.7 million of TDRs in accrual status compared to \$4.9 million of TDRs in nonaccrual status and \$7.1 million of TDRs in accrual status at December 31, 2010. Approximately \$2.1 million and \$1.3 million in specific reserves have been established for these loans as of September 30, 2011 and December 31, 2010, respectively.

During the nine months ending September 30, 2011, the terms of 27 loans were modified in troubled debt restructurings, of which 19 were related to commercial loans that were already placed on nonaccrual. Nonaccruing restructured loans remain in nonaccrual status until there has been a period of sustained repayment performance for a reasonable period, usually six months. The remaining eight loans represented residential and consumer loans. Our concessions on restructured loans consisted mainly of forbearance agreements, reduction in interest rates or extensions of maturities. Principal balances are generally not forgiven by us when a loan is modified as a TDR.

The following table presents loans identified as TDRs during the three and nine months ended September 30, 2011:

(In Thousands)	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2011
Commercial	\$ 746	\$ 1,352
Commercial mortgages	2,170	7,725
Construction	189	13,909
Residential	-	2,335
Consumer	146	146
Total	\$ 3,251	\$ 25,467

The troubled debt restructurings described above increased the allowance for loan losses by \$1.2 million through allocation of a specific reserve, and resulted in charge offs of \$10.3 million during the nine months ending September 30, 2011, most of which had been previously identified and reserved for in prior periods.

The following table summarizes TDRs which have defaulted (defined as past due 90 days) during the three and nine months ended September 30, 2011 that were restructured within the last twelve months prior to September 30, 2011:

(In Thousands)	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2011
Commercial	\$ -	\$ -
Commercial mortgages	-	-
Construction	-	-
Residential	162	162
Consumer	-	-
Total	\$ 162	\$ 162

6. COMPREHENSIVE INCOME

The following schedule reconciles net income to total comprehensive income:

	For the three months ended September 30, (In Thousands)		For the nine months ended September 30, (In Thousands)	
	2011	2010	2011	2010
Net income	\$6,786	\$8,222	\$16,515	\$12,037
Other Comprehensive Income:				
Other, net	—	162	—	162
Unrealized holding gains on securities available-for-sale arising during the period	8,568	1,105	9,321	18,590
Tax expense	(3,230)	(420)	(3,516)	(7,064)
Net of tax amount	5,338	685	5,805	11,526
Total comprehensive income	\$12,124	\$9,069	\$22,320	\$23,725

7. TAXES ON INCOME

We account for income taxes in accordance with FASB ASC 740, Income Taxes (“ASC 740”) (Formerly SFAS No. 109, Accounting for Income Taxes and FASB Interpretation No. 48, Accounting for Uncertainty In Income Taxes, an Interpretation of FASB Statement 109). ASC 740 requires the recording of deferred income taxes that reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. We exercise significant judgment in the evaluation of the amount and timing of the recognition of the resulting tax assets and liabilities. The judgments and estimates required for the evaluation are updated based upon changes in business factors and the tax laws. If actual results differ from the assumptions and other considerations used in estimating the amount and timing of tax recognized, there can be no assurance that additional expenses will not be required in future periods. No valuation allowance has been recorded on our deferred tax assets due to our history of prior earnings along with our expectations of future income. ASC 740 prescribes a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized. We recognize, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the financial statements. Assessment of uncertain tax positions under ASC 740 requires careful consideration of the technical merits of a position based on our analysis of tax regulations and interpretations.

The total amount of unrecognized tax benefits as of September 30, 2011 and December 31, 2010 were \$100,000 and \$1.0 million, respectively, of which \$100,000 would affect our September 30, 2011 effective tax rate if recognized. During the quarter ended September 30, 2011 we recorded tax benefits of \$376,000 through earnings that resulted from a decrease in our income tax reserve primarily due to the expiration of a statute of limitations on a certain tax item. Further, we recorded tax benefits of \$500,000 through equity during the quarter ended September 30, 2011 for a similar statute of limitations related decrease in the income tax reserve. The nine months ended September 30, 2010 included tax benefits of \$899,000 resulting from a decrease in our income tax reserve due to the expiration of the statute of limitations on certain tax items. As of September 30, 2011 and December 31, 2010, the total amount of accrued interest included in such unrecognized tax benefits were \$18,000 and \$51,000, respectively. Penalties of \$6,000 are included in such unrecognized tax benefits. We record interest and penalties on potential income tax deficiencies as income tax expense. Our Federal and state tax returns for the 2008 through 2010 tax years are subject

to examination as of September 30, 2011. There are currently no income tax audits in process.

8. SEGMENT INFORMATION

Under the definition of FASB ASC 280, Segment Reporting (“ASC 280”) (formerly SFAS No. 131, Disclosures About Segments of an Enterprise and Related Information) we discuss our business in three segments. There is one segment for each of WSFS Bank (including WSFS Investment Group, Inc.), Cash Connect, (the ATM division of WSFS), and Trust and Wealth Management. Trust and Wealth Management combines Montchanin and Christiana Trust into a single reportable segment.

The WSFS Bank segment provides financial products to commercial and retail customers through its 49 offices located in Delaware (39), Pennsylvania (8), Virginia (1) and Nevada (1). Retail and Commercial Banking, Commercial Real Estate Lending, Private Banking and other banking business units (including the reorganization of WSFS Investment Group, Inc.) are operating departments of WSFS. These departments share the same regulator, the same market, many of the same customers and provide similar products and services through the general infrastructure of the Bank. Because of these and other reasons, these departments are not considered discrete segments and are appropriately aggregated within our WSFS Bank segment in accordance with ASC 280.

Cash Connect provides turnkey ATM services through strategic partnerships with several of the largest networks, manufacturers and service providers in the ATM industry. The balance sheet category “Cash in non-owned ATMs” includes cash from which fee income is earned through bailment arrangements with customers of Cash Connect.

The Trust and Wealth Management segment is comprised of Christiana Trust and Montchanin. Christiana Trust was acquired as part of the acquisition of CB&T in December 2010 and WSFS’ Trust and Wealth Management business was consolidated into Christiana Trust. Christiana Trust provides investment, fiduciary, agency and commercial domicile services from locations in Delaware and Nevada. These services are provided to individuals and families, as well as corporations and institutions. The Christiana Trust division provides these services to local, national and international customers. Montchanin has one consolidated wholly owned subsidiary, Cypress Capital Management, LLC (Cypress). Cypress is a Wilmington-based investment advisory firm serving high net-worth individuals and institutions.

An operating segment is a component of an enterprise that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the enterprise’s chief operating decision makers to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. We evaluate performance based on pretax ordinary income relative to resources used, and allocate resources based on these results. The accounting policies applicable to our segments are the same that apply to the preparation of our accompanying Consolidated Financial Statements. Segment information for the three and nine months ended September 30, 2011 and 2010 was as follows:

For the three months ended September 30, 2011

	WSFS Bank	Cash Connect	Trust & Wealth Management	Total
	(In Thousands)			
External customer revenues:				
Interest income	\$40,091	\$-	\$ -	\$40,091
Noninterest income	9,701	4,235	2,988	16,924
Total external customer revenues	49,792	4,235	2,988	57,015
Inter-segment revenues:				
Interest income	349	-	876	1,225
Noninterest income	754	202	-	956
Total inter-segment revenues	1,103	202	876	2,181
Total revenue	50,895	4,437	3,864	59,196
External customer expenses:				
Interest expense	7,911	-	-	7,911
Noninterest expenses	27,867	2,187	2,358	32,412
Provision for loan loss	6,558	-	-	6,558
Total external customer expenses	42,336	2,187	2,358	46,881
Inter-segment expenses				
Interest expense	876	349	-	1,225
Noninterest expenses	202	358	396	956
Total inter-segment expenses	1,078	707	396	2,181
Total expenses	43,414	2,894	2,754	49,062
Income before taxes	\$7,481	\$1,543	\$ 1,110	\$10,134
Provision for income taxes				3,348
Consolidated net income				\$6,786
Capital expenditures	\$2,374	\$837	\$ 2	\$3,213
As of September 30, 2011				
Cash and cash equivalents	\$77,310	\$383,358	\$ 2,885	\$463,553
Other segment assets	3,692,851	22,148	10,188	3,725,187
Total segment assets	\$3,770,161	\$405,506	\$ 13,073	\$4,188,740

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For the three months ended September 30, 2010

	WSFS Bank	Cash Connect	Trust & Wealth Management	Total
	(In Thousands)			
External customer revenues:				
Interest income	\$40,579	\$-	\$ -	\$40,579
Noninterest income	10,172	3,523	730	14,425
Total external customer revenues	50,751	3,523	730	55,004
Inter-segment revenues:				
Interest income	238	-	-	238
Noninterest income	701	202	-	903
Total inter-segment revenues	939	202	-	1,141
Total revenue	51,690	3,725	730	56,145
External customer expenses:				
Interest expense	10,402	-	-	10,402
Noninterest expenses	23,916	(2,643)	819	22,092
Provision for loan loss	9,976	-	-	9,976
Total external customer expenses	44,294	(2,643)	819	42,470
Inter-segment expenses				
Interest expense	-	238	-	238
Noninterest expenses	202	377	324	903
Total inter-segment expenses	202	615	324	1,141
Total expenses	44,496	(2,028)	1,143	43,611
Income (loss) before taxes	\$7,194	\$5,753	\$ (413)	\$12,534
Provision for income taxes				4,312
Consolidated net income				\$8,222
Capital expenditures	\$1,463	\$122	\$ 2	\$1,587
As of December 31, 2010				
Cash and cash equivalents	\$62,383	\$271,168	\$ 1,244	\$334,795
Other segment assets	3,450,091	13,311	673	3,464,075
Total segment assets	\$3,512,474	\$284,479	\$ 1,917	\$3,798,870

For the nine months ended September 30, 2011

	WSFS Bank	Cash Connect	Trust & Wealth Management	Total
	(In Thousands)			
External customer revenues:				
Interest income	\$ 119,057	\$ -	\$ -	\$ 119,057
Noninterest income	27,117	11,484	7,991	46,592
Total external customer revenues	146,174	11,484	7,991	165,649
Inter-segment revenues:				
Interest income	913	-	3,132	4,045
Noninterest income	2,486	524	-	3,010
Total inter-segment revenues	3,399	524	3,132	7,055
Total revenue	149,573	12,008	11,123	172,704
External customer expenses:				
Interest expense	25,436	-	-	25,436
Noninterest expenses	81,101	5,824	7,526	94,451
Provision for loan loss	21,048	-	-	21,048
Total external customer expenses	127,585	5,824	7,526	140,935
Inter-segment expenses				
Interest expense	3,132	913	-	4,045
Noninterest expenses	524	1,162	1,324	3,010
Total inter-segment expenses	3,656	2,075	1,324	7,055
Total expenses	131,241	7,899	8,850	147,990
Income before taxes	\$ 18,332	\$ 4,109	\$ 2,273	\$ 24,714
Income tax provision				8,199
Consolidated net income				\$ 16,515
Capital expenditures	\$ 6,768	\$ 1,014	\$ 308	\$ 8,090
As of September 30, 2011				
Cash and cash equivalents	\$ 77,310	\$ 383,358	\$ 2,885	\$ 463,553
Other segment assets	3,692,851	22,148	10,188	3,725,187
Total segment assets	\$ 3,770,161	\$ 405,506	\$ 13,073	\$ 4,188,740

For the nine months ended September 30, 2010

	WSFS Bank	Cash Connect	Trust & Wealth Management	Total
	(In Thousands)			
External customer revenues:				
Interest income	\$ 122,591	\$ -	\$ -	\$ 122,591
Noninterest income	25,794	9,983	2,225	38,002
Total external customer revenues	148,385	9,983	2,225	160,593
Inter-segment revenues:				
Interest income	685	-	-	685
Noninterest income	2,130	577	-	2,707
Total inter-segment revenues	2,815	577	-	3,392
Total revenue	151,200	10,560	2,225	163,985
External customer expenses:				
Interest expense	32,373	-	-	32,373
Noninterest expenses	72,470	4,470	2,524	79,464
Provision for loan loss	31,980	-	-	31,980
Total external customer expenses	136,823	4,470	2,524	143,817
Inter-segment expenses				
Interest expense	-	685	-	685
Noninterest expenses	577	1,110	1,020	2,707
Total inter-segment expenses	577	1,795	1,020	3,392
Total expenses	137,400	6,265	3,544	147,209
Income (loss) before taxes	\$ 13,800	\$ 4,295	\$ (1,319)	\$ 16,776
Income tax provision				4,739
Consolidated net income				\$ 12,037
Capital expenditures	\$ 4,533	\$ 129	\$ 2	\$ 4,664
As of December 31, 2010				
Cash and cash equivalents	\$ 62,383	\$ 271,168	\$ 1,244	\$ 334,795
Other segment assets	3,450,091	13,311	673	3,464,075
Total segment assets	\$ 3,512,474	\$ 284,479	\$ 1,917	\$ 3,798,870

9. FAIR VALUE OF FINANCIAL INSTRUMENTS

The reported fair values of financial instruments are based on a variety of factors. In certain cases, fair values represent quoted market prices for identical or comparable instruments. In other cases, fair values have been estimated based on assumptions regarding the amount and timing of estimated future cash flows that are discounted to reflect current market rates and varying degrees of risk. Accordingly, the fair values may not represent actual values of the financial instruments that could have been realized as of period-end or that will be realized in the future.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and Short-Term Investments: For cash and short-term investments, including due from banks, federal funds sold, securities purchased under agreements to resell and interest-bearing deposits with other banks, the carrying amount is a reasonable estimate of fair value.

Investments and Mortgage-Backed Securities: Fair value of investment and mortgage-backed securities is based on quoted market prices, where available. If a quoted market price is not available, fair value is estimated using quoted prices for similar securities or through internally developed models. The fair value of our investment in reverse mortgages is based on the net present value of estimated cash flows, which have been updated to reflect recent external appraisals of the underlying collateral. For additional discussion of our mortgage-backed securities-trading or our internally developed models, see Note 10, Fair Value of Financial Assets, to the Consolidated Financial Statements.

Loans: Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type: commercial, commercial mortgages, construction, residential mortgages and consumer. For loans that repriced frequently, the book value approximates fair value. The fair values of other types of loans are estimated by discounting expected cash flows using the current rates at which similar loans would be made to borrowers with comparable credit ratings and for similar remaining maturities. The fair value of nonperforming loans is based on recent external appraisals of the underlying collateral. Estimated cash flows, discounted using a rate commensurate with current rates and the risk associated with the estimated cash flows, are utilized if appraisals are not available. This technique does not contemplate an exit price.

Bank-Owned Life Insurance: The estimated fair value approximates the book value for this investment.

Stock in the Federal Home Loan Bank of Pittsburgh: The fair value of FHLB stock is assumed to be essentially equal to its cost. We carry FHLB stock at cost, or par value, and evaluate FHLB stock for impairment based on the ultimate recoverability of par value rather than by recognizing temporary declines in value. As part of the impairment assessment of FHLB stock, management considers, among other things, (i) the significance and length of time of any declines in net assets of the FHLB compared to its capital stock, (ii) commitments by the FHLB to make payments required by law or regulations and the level of such payments in relation to its operating performance, (iii) the impact of legislative and regulatory changes on FHLB, the FHLB has access to the U.S. Government-Sponsored Enterprise Credit Facility, a secured lending facility that serves as a liquidity backstop, substantially reducing the likelihood that the FHLB would need to sell securities to raise liquidity and, thereby, cause the realization of large economic losses. On August 8, 2011, Standard & Poors (“S&P”) downgraded the FHLB from AAA to AA+, similar to their downgrade of the U.S. sovereign rating. The reduction in the FHLB credit rating was due to the belief, by S&P, that the FHLB system is certain to receive U.S. government support, if necessary, resulting from the important role the FHLB system plays as primary liquidity providers to U.S. mortgage and housing-market participants. Despite the downgrade, the FHLB continues to have a very high degree of government support and was in compliance with all regulatory capital requirements as of September 30, 2011. As a result, we have determined there was no

other-than-temporary impairment related to our FHLB stock investment as of September 30, 2011.

Demand Deposits, Savings Deposits and Time Deposits: The fair value of demand deposits and savings deposits is determined by projecting future cash flows using an estimated economic life based on account characteristics. The resulting cash flow is discounted using rates available on alternative funding sources. The fair value of time deposits is estimated using the rate and maturity characteristics of the deposits to estimate their cash flow. The cash flow is discounted at rates for similar term wholesale funding.

Borrowed Funds: Rates currently available to us for debt with similar terms and remaining maturities are used to estimate fair value of existing debt.

Off-Balance Sheet Instruments: The fair value of off-balance sheet instruments, including commitments to extend credit and standby letters of credit, is estimated using the fees currently charged to enter into similar agreements with comparable remaining terms and reflects the present creditworthiness of the counterparties.

The book value and estimated fair value of our financial instruments are as follows:

(In Thousands)	September 30, 2011		December 31, 2010	
	Book Value	Fair Value	Book Value	Fair Value
Financial assets:				
Cash and cash equivalents	\$463,553	\$463,553	\$376,759	\$376,759
Investment securities	48,092	48,093	52,451	52,428
Mortgage-backed securities	784,940	784,940	713,358	713,358
Loans, net	2,650,005	2,691,521	2,575,890	2,586,669
Stock in Federal Home Loan Bank of Pittsburgh	37,638	37,638	37,536	37,536
Accrued interest receivable	11,326	11,326	11,765	11,765
Financial liabilities:				
Deposits	2,952,053	2,906,435	2,810,744	2,826,515
Borrowed funds	805,070	806,989	747,606	751,970
Accrued interest payable	8,533	8,533	3,317	3,317

The estimated fair value of our off-balance sheet financial instruments is as follows:

(In Thousands)	September	December
	30, 2011	31, 2010
Off-balance sheet instruments:		
Commitments to extend credit	\$4,186	\$3,729
Standby letters of credit	108	210

10. FAIR VALUE OF FINANCIAL ASSETS

Effective January 1, 2008, we adopted the provisions of FASB ASC 820-10 (“ASC 820-10”) (formerly SFAS No. 157, Fair Value Measurements and Financial Accounting Standards Board Staff Position (FSP) No. 157-2, Effective Date of FASB Statement No. 157), for financial assets and financial liabilities. This adoption did not have a material impact on our financial statements.

ASC 820-10 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820-10 establishes a fair value hierarchy that prioritizes the use of inputs used in valuation methodologies into the following three levels:

Level 1: Inputs to the valuation methodology are quoted prices, unadjusted, for identical assets or liabilities in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; inputs to the valuation methodology include quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs to the valuation methodology that are derived principally from or can be corroborated by

observable market data by correlation or other means.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Level

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3 assets and liabilities include financial instruments whose value is determined using discounted cash flow methodologies, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. The table below presents the balances of assets measured at fair value as of September 30, 2011 (there are no material liabilities measured at fair value):

Description	Quoted Prices in Active Markets for Identical Asset (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
(in Thousands)				
Assets Measured at Fair Value on a Recurring Basis				
Available-for-sale securities:				
Collateralized mortgage obligations	\$ —	\$ 330,431	\$ 3,616	\$ 334,047
FNMA	—	302,886	—	302,886
FHLMC	—	74,255	—	74,255
GNMA	—	61,320	—	61,320
U.S. Government and agencies	—	44,095	—	44,095
State and political subdivisions	—	4,196	—	4,196
Reverse mortgages	—	—	(418)	(418)
Trading Securities	—	—	12,432	12,432
Total assets measured at fair value on a recurring basis	\$ —	\$ 817,183	\$ 15,630	\$ 832,813
Assets Measured at Fair Value on a Nonrecurring Basis				
Other real estate owned	\$ —	\$ 11,880	\$ —	\$ 11,880
Impaired Loans (collateral dependent)	—	76,772	—	76,772
Total assets measured at fair value on a nonrecurring basis	\$ —	\$ 88,652	\$ —	\$ 88,652

The table below presents the balances of assets measured at fair value as of December 31, 2010 (there are no material liabilities measured at fair value):

Description	Quoted Prices in Active Markets for Identical Asset (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
(in Thousands)				
Assets Measured at Fair Value on a Recurring Basis				
Available-for-sale securities:				
Collateralized mortgage obligations	\$ —	\$ 500,034	\$ —	\$ 500,034
FNMA	—	90,048	—	90,048
FHLMC	—	44,440	—	44,440
GNMA	—	66,404	—	66,404
U.S. Government and agencies	—	50,003	—	50,003
State and political subdivisions	—	2,915	—	2,915
Reverse mortgages	—	—	(686)	(686)
Trading Securities	—	—	12,432	12,432
Total assets measured at fair value on a recurring basis	\$ —	\$ 753,844	\$ 11,746	\$ 765,590
Assets Measured at Fair Value on a Nonrecurring Basis				
Other real estate owned	\$ —	\$ 9,024	\$ —	\$ 9,024
Impaired Loans (collateral dependent)	—	71,805	—	71,805
Total assets measured at fair value on a nonrecurring basis	\$ —	\$ 80,829	\$ —	\$ 80,829

Fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models or obtained from third parties that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include unobservable parameters. Our valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While we believe our valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Available-for-sale securities. As of September 30, 2011, securities classified as available for sale are reported at fair value using both Level 2 and Level 3 inputs. Included in the Level 2 total are approximately \$44.1 million in Federal Agency debentures, \$587.5 million in Federal Agency MBS, \$181.4 million of Private Label MBS, and \$4.2 million in municipal bonds. Agency and MBS securities are predominately AAA-rated. We believe that this Level 2 designation is appropriate for these securities under ASC 820-10 as, with almost all fixed income securities, none are exchange traded, and all are priced by correlation to observed market data. For these securities we obtain fair value measurements from an independent pricing service. The fair value measurements consider observable data that may

include dealer quotes, market spreads, cash flows, U.S. government and agency yield curves, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the security's terms and conditions, among other factors. Included in the Level 3 total is a small equity tranche of a reverse mortgage security purchased on July 15, 2011. This security is Level 3 because there is no active market for this security and no observable inputs that reflect quoted prices for identical assets in active markets (Level 1) or inputs other than quoted prices that are observable for the asset through corroboration with observable market data (Level 2). In order to establish the fair value for a Level 3 asset a "mark-to-model" has been developed using the income

approach described in ASC 820-10-35-32 and is similar to the methodology used to value our trading securities described below.

Trading securities. The amount included in the trading securities category represents the fair value of a BBB-rated tranche of a reverse mortgage security. There has never been an active market for these securities. As such, we classify these trading securities as Level 3 under ASC 820-10. As prescribed by ASC 820-10 management used various observable and unobservable inputs to develop a range of likely fair value prices where this security would be exchanged in an orderly transaction between market participants at the measurement date. The unobservable inputs reflect management's assumptions about the assumptions that market participants would use in pricing this asset. Included in these inputs were the median of a selection of other BBB-rated securities as well as quoted market prices from higher rated tranches of this asset class. As a result, the value assigned to this security is determined primarily through a discounted cash flow analysis. All of these assumptions require a significant degree of management judgment.

Reverse Mortgages. The amount of our investment in reverse mortgages represents the estimated value of future cash flows of the reverse mortgages at a rate deemed appropriate for these mortgages, based on the market rate for similar collateral. The projected cash flows depend on assumptions about life expectancy of the mortgagor and the future changes in collateral values. Due to the significant amount of management judgment and the unobservable input calculations, these reverse mortgages have been classified as Level 3.

The changes in Level 3 assets measured at fair value are summarized as follows:

(In Thousands)	Trading Securities	Reverse Mortgages	Available- for-sale Securities	Total
Balance at December 31, 2009	\$12,183	\$(530)	\$—	\$11,653
Total net income (losses) for the period included in net income	249	(287)	—	(38)
Purchases, sales, issuances, and settlements, net	—	131	—	131
Balance at December 31, 2010	\$12,432	\$(686)	—	\$11,746
Total net income (losses) for the period included in net income	—	(128)	120	(8)
Purchases, sales, issuances, and settlements, net	—	396	2,629	3,025
Mark-to-market adjustment	—	—	867	867
Balance at September 30, 2011	\$12,432	\$(418)	\$3,616	\$15,630

Other real estate owned. Other real estate owned consists of loan collateral which has been repossessed through foreclosure or other measures. Initially, foreclosed assets are recorded as held for sale at the lower of the loan balance or fair value of the collateral less estimated selling costs. Subsequent to foreclosure, valuations are updated periodically and the assets may be marked down further, reflecting a new cost basis. The fair value of our real estate owned was estimated using Level 2 inputs based on appraisals obtained from third parties.

Impaired loans. Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a gross amount of \$84.1 million and \$83.8 million at September 30, 2011 and December 31, 2010, respectively. The valuation allowance on impaired loans was \$7.3 million as of September 30, 2011 and \$12.0 million as of December 31, 2010. During the three and nine months ended September 30, 2011, we recorded net decreases of \$1.7 million and \$4.7 million, respectively, in our allowance for loan loss as a result of adjusting the carrying value and estimated fair value on these collateral dependent impaired loans.

11. INDEMNIFICATIONS AND GUARANTEES

Secondary Market Loan Sales. We generally do not sell loans with recourse except to the extent arising from standard loan sale contract provisions covering violations of representations and warranties and, under certain circumstances first payment defaults by borrowers. These are customary repurchase provisions in the secondary market for conforming mortgage loan sales. These indemnifications may include our repurchase of the loans. Repurchases and losses are rare, and no provision is made for the losses at the time of sale. During the third quarter of 2011, we had no repurchases under these indemnifications.

We typically sell fixed-rate, conforming first mortgage loans (including reverse mortgages) in the secondary market as part of our ongoing asset/liability management program. Loans held-for-sale are carried at the lower of cost or market of the aggregate or in some cases individual loans. Gains and losses on sales of loans are recognized at the time of the sale.

Swap Guarantees. We entered into agreements with three unrelated financial institutions whereby those financial institutions entered into interest rate derivative contracts (interest rate swap transactions) with customers referred to them by us. By the terms of the agreements, those financial institutions have recourse to us for any exposure created under each swap transaction in the event the customer defaults on the swap agreement and the agreement is in a paying position to the third-party financial institution. This is a customary arrangement that allows smaller financial institutions like us to provide access to interest rate swap transactions for our customers without creating the swap ourselves.

At September 30, 2011 there were 71 variable-rate swap transactions between the third party financial institutions and our customers, compared to 57 at December 31, 2010. The initial notional amount aggregated approximately \$289.1 million at September 30, 2011 compared with \$236.1 million at December 31, 2010. At September 30, 2011 maturities ranged from approximately one year to 14 years. The aggregate market value of these swaps to the customers was a liability of \$32.3 million at September 30, 2011 and \$16.9 million at December 31, 2010. No reserves are needed for these guarantees as it is not probable that we would have any contingent liability for a loss on the obligations.

12. ASSOCIATE (EMPLOYEE) BENEFIT PLANS

Postretirement Benefits

We share certain costs of providing health and life insurance benefits to retired Associates (and their eligible dependents). Substantially all Associates may become eligible for these benefits if they reach normal retirement age while working for us.

We account for our obligations under the provisions of FASB ASC 715, Compensation – Retirement Benefits (“ASC 715”) (Formerly SFAS No. 106, Employers’ Accounting for Postretirement Benefits Other Than Pensions). ASC 715 requires that the costs of these benefits be recognized over an Associate’s active working career. Disclosures are in accordance with ASC 715.

The following disclosures of the net periodic benefit cost components of postretirement benefits were measured at January 1, 2011 and 2010:

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2011	2010	2011	2010
(In Thousands)				
Service cost	\$52	\$43	\$156	\$128
Interest cost	41	38	125	114
Amortization of transition obligation	15	15	45	45
Net loss recognition	8	3	24	9
Net periodic benefit cost	\$116	\$99	\$350	\$296

13. NONINTEREST EXPENSES

During the nine months ended September 30, 2011 and 2010, we recorded \$780,000 (including \$334,000 in the first quarter of 2011 and \$446,000 in the second quarter of 2011) and \$311,000 (including \$168,000 in the second quarter of 2010 and \$143,000 in the third quarter of 2010), respectively, in non-routine charges related to the acquisition and integration of Christiana Bank & Trust. These expenses mainly reflected salaries, benefits and other compensation, data processing and operations expenses and professional fees.

During the nine months ended September 30, 2010, we recorded a \$4.5 million non-routine charge and subsequent complete recovery. On February 19, 2010, we reported in a regulatory filing that an executive of an armored car company

that served as a vendor for several of Cash Connect's customers, engaged in embezzlement. In the first quarter of 2010, we recorded a \$4.5 million loss related to funds not immediately recoverable by Cash Connect. These funds were fully recovered during the third quarter of 2010.

14. STOCK AND COMMON STOCK WARRANTS

In August 2010, we completed an underwritten public offering of 1,370,000 shares of common stock. The offering was priced at \$36.50 per share, a slight premium to the prior day's closing price, and raised \$47.1 million net of \$2.9 million of costs.

On September 24, 2009 we completed a private placement of stock to Peninsula Investment Partners, L.P., pursuant to which we issued and sold 862,069 shares of common stock for a total purchase price of \$25.0 million, and a 10-year warrant to purchase 129,310 shares of common stock at an exercise price of \$29.00 per share. The warrant is immediately exercisable.

Total proceeds of \$25.0 million were allocated, based on the relative fair value of the common stock and common stock warrants, to common stock for \$23.5 million and common stock warrants for \$1.5 million on September 24, 2009.

On January 23, 2009, we entered into a purchase agreement with the U.S. Treasury pursuant to which we issued and sold 52,625 shares of our fixed-rate cumulative perpetual preferred stock for a total purchase price of \$52.6 million, and a 10-year warrant to purchase 175,105 shares of common stock at an exercise price of \$45.08 per share. We will pay the Treasury Department a five percent dividend annually for each of the first five years of the investment and a nine percent dividend thereafter until the shares are redeemed. The cumulative dividend for the preferred stock is accrued for and payable on February 15, May 15, August 15 and November 15 of each year. We declared and paid \$2.0 million in preferred stock dividends during the nine months ended September 30, 2011.

Based on the relative fair value of the preferred stock and common stock warrants on January 23, 2009, the total proceeds of \$52.6 million were allocated to preferred stock for \$51.9 million and common stock for \$693,000. The preferred stock discount is being accreted, on an effective yield method, to preferred stock over five years. We have accreted a total of \$104,000 during the nine months ended September 30, 2011, relating to the discount on preferred stock.

The preferred stock is nonvoting, except for class voting rights on certain matters that could adversely affect the shares. They may be redeemed by us for the liquidation preference (\$1,000 per share), plus accrued but unpaid dividends, with the Treasury's approval. The warrant is exercisable immediately and subject to certain anti-dilution and other adjustments.

15. GOODWILL

On December 3, 2010, we completed the acquisition of CB&T for a cash purchase price of \$34.5 million. The acquisition of CB&T was accounted for using the acquisition method of accounting and, accordingly, assets acquired and liabilities assumed were recorded at their estimated fair values as of the acquisition date. The excess cash paid over the fair value of net assets acquired was recorded as goodwill in the amount of \$17.3 million, which, for tax purposes is being amortized over 15 years, as we have made an election for income tax purposes to treat the acquisition as a taxable purchase of assets. We also recorded \$3.1 million of other intangible assets and \$1.9 million in core deposit intangibles ("CDI"). The intangible assets are being amortized over periods ranging from 2 to 7.5 years using straight-line methods and the CDI is being amortized over a period of 10 years using a declining balance method. Both of these items are also being amortized over 15 years for tax purposes. The goodwill and intangibles

have been allocated between the WSFS Bank and Trust and Wealth Management segments.

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The following table details the effect on goodwill from the changes in estimates of the fair values of the assets acquired and liabilities assumed from the amounts originally reported on the Form 10-K for the year ended December 31, 2010 (in thousands):

Goodwill resulting from CB&T acquisition reported on Form 10-K for the year ended December 31, 2010	\$ 15,876
Effect of adjustments to:	
Loans	801
Premises and equipment	250
Other liabilities, net	350
Adjusted goodwill resulting from acquisition of CB&T as of September 30, 2011	\$ 17,277

16. LEGAL PROCEEDINGS

As disclosed in previous filings, we were served with a complaint filed in U.S. Bankruptcy Court by a bankruptcy trustee relating to a former WSFS Bank customer. The complaint challenges the Bank's actions in exercising its rights concerning an outstanding loan and also seeks to avoid and recover the pre-bankruptcy repayment of that loan. Management of the Bank believes it acted appropriately and will vigorously defend itself against the complaint. No litigation reserve has been recorded as it is not yet possible to establish the probability of or reasonably estimate a potential loss. Our insurance carrier has preliminarily determined our future litigation defense costs are covered by an insurance policy we have for such matters.

ITEM 2. MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

WSFS Financial Corporation is parent to Wilmington Savings Fund Society, FSB (“WSFS Bank” or the “Bank”), the seventh oldest bank and trust in the United States continuously operating under the same name. A permanent fixture in the community, WSFS has been in operation for more than 179 years. In addition to its focus on stellar customer service, the Bank has continued to fuel growth and remain a leader in our community. We are a relationship-focused, locally-managed, community banking institution that has grown to become the largest thrift holding company in the State of Delaware, one of the top commercial lenders in the state, the third largest bank in terms of Delaware deposits and one of the top 100 trust companies in the country. We state our mission simply: We Stand for Service and Strengthening Our Communities.

Our core banking business is commercial lending funded by customer-generated deposits. We have built a \$2.1 billion commercial loan portfolio by recruiting the best seasoned commercial lenders in our markets and offering a high level of service and flexibility typically associated with a community bank. We fund this business primarily with deposits generated through commercial relationships and retail deposits. We service our customers primarily from our 48 offices located in Delaware (38), Pennsylvania (8), Virginia (1) and Nevada (1). We also offer a broad variety of consumer loan products, retail securities and insurance brokerage through our retail branches.

We have two consolidated subsidiaries, WSFS Bank and Montchanin Capital Management, Inc. (“Montchanin”) and one unconsolidated affiliate, WSFS Capital Trust III (“the Trust”).

WSFS Bank has two wholly owned subsidiaries, WSFS Investment Group, Inc. and Monarch Entity Services, LLC (“Monarch”). WSFS Investment Group, Inc., markets various third-party investment and insurance products, such as single-premium annuities, whole life policies and securities primarily through the Bank’s retail banking system and directly to the public. Monarch provides commercial domicile services which include employees, directors, sublease of office facilities and registered agent services in Delaware and Nevada.

Our Cash Connect division is a premier provider of ATM Vault Cash and related services in the United States. Cash Connect manages nearly \$400 million in vault cash in more than 11,500 ATMs nationwide and also provides online reporting and ATM cash management, predictive cash ordering, armored carrier management, ATM processing and equipment sales. Cash Connect also operates over 400 ATMs for WSFS Bank, which has, by far, the largest branded ATM network in Delaware.

In 2010 we acquired Christiana Bank & Trust Company (“CB&T”) and established our Christiana Trust division. The Christiana Trust division provides investment, fiduciary, agency and commercial domicile services to local, national and international customers by making use of the advantages of its facilities in Delaware and Nevada. These services are provided to individuals and families, as well as corporations and institutions.

Montchanin provides asset management services in our primary market area through its wholly owned subsidiary, Cypress Capital Management, LLC (“Cypress”). Cypress is a Wilmington-based investment advisory firm servicing high net-worth individuals and institutions.

Combined, the Christiana Trust division and Montchanin service approximately \$9.3 billion in fiduciary assets, including approximately \$1 billion in assets under management at September 30, 2011.

Until July 21, 2011, WSFS Financial Corporation and WSFS Bank were regulated by the Office of Thrift Supervision. As of July 21, 2011, WSFS Financial Corporation's primary federal regulator became the Federal Reserve and WSFS Bank's primary federal regulator became the Office of the Comptroller of the Currency. While we do not anticipate the change in primary regulators will have a material impact on our operations, there can be no assurance that the interpretation by these agencies of the regulations governing our business will not be different than that of the Office of Thrift Supervision which may affect the manner in which we conduct our business in the future.

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, and exhibits thereto, contains estimates, predictions, opinions, projections and other statements that may be interpreted as “forward-looking statements” as that phrase is defined in the Private Securities Litigation Reform Act of 1995. Such statements include, without limitation, references to our financial goals, management’s plans and objectives for future operations, financial and business trends, business prospects, and management’s outlook or expectations for earnings, revenues, expenses, capital levels, liquidity levels, asset quality or other future financial or business performance, strategies or expectations. Such forward-looking statements are based on various assumptions (some of which may be beyond the Company’s control) and are subject to risks and uncertainties (which change over time) and other factors which could cause actual results to differ materially from those currently anticipated. Such risks and uncertainties include, but are not limited to, those related to the economic environment, particularly in the market areas in which the Company operates; the volatility of the financial and securities markets, including changes with respect to the market value of financial assets; changes in market interest rates, changes in government regulation affecting financial institutions, including the Dodd-Frank Wall Street Reform and Consumer Protection Act and the rules being issued in accordance with this statute and potential expenses associated therewith; changes resulting from our participation in the CPP including additional conditions that may be imposed in the future on participating companies; and the costs associated with resolving any problem loans and other risks and uncertainties, discussed in documents filed by WSFS Financial Corporation with the Securities and Exchange Commission from time to time. Forward looking statements are as of the date they are made, and the Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company.

CRITICAL ACCOUNTING POLICIES

The discussion and analysis of the financial condition and results of operations are based on the Consolidated Financial Statements, which are prepared in conformity with U.S. generally accepted accounting principles. The preparation of these Consolidated Financial Statements requires us to make estimates and assumptions affecting the reported amounts of assets, liabilities, revenue and expenses. We regularly evaluate these estimates and assumptions including those related to the allowance for loan losses, deferred taxes, fair value measurements, goodwill and other intangible assets. We base our estimates on historical experience and various other factors and assumptions that are believed to be reasonable under the circumstances. These form the basis for making judgments on the carrying value of assets and liabilities that are not readily apparent from other sources. Although our current estimates contemplate current economic conditions and how we expect them to change in the future, for the remainder of 2011, it is reasonably possible that actual conditions may be worse than anticipated in those estimates, which could materially affect our results of operations and financial condition. Actual results may differ from these estimates under different assumptions or conditions.

The following are critical accounting policies that involve more significant judgments and estimates. See further discussion of these critical accounting policies in the 2010 Annual Report on Form 10-K.

Allowance for Loan Losses

We maintain allowances for loan losses and charge losses to these allowances when realized. We consider the determination of the allowance for loan losses to be critical because it requires significant judgment reflecting our best estimate of impairment related to specifically evaluated impaired loans as well as the inherent risk of loss for those in the remaining loan portfolio. Our evaluation is based upon a continuing review of the portfolio, with consideration given to evaluations resulting from examinations performed by regulatory authorities.

Deferred Taxes

We account for income taxes in accordance with Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 740, Income Taxes (“ASC 740”), which requires the recording of deferred income taxes that reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. We consider our accounting policies on deferred taxes to be critical because we regularly assess the need for valuation allowances on deferred income tax assets that may result from, among other things, limitations imposed by Internal Revenue Code and uncertainties, including the timing of settlement and realization of these differences. No valuation allowance is required as of September 30, 2011.

Fair Value Measurements

We adopted FASB ASC 820-10 Fair Value Measurements and Disclosures (“ASC 820”), which defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. We consider our accounting policies related to fair value measurements to be critical because they are important to the portrayal of our financial condition and results, and they require our subjective and complex judgment as a result of the need to make estimates about the effects of matters that are inherently uncertain. See Note 10-Fair Value of Financial Assets to our Consolidated Financial Statements.

Goodwill and Other Intangible Assets

In accordance with FASB ASC 805, Business Combinations, and FASB ASC 350, Intangibles—Goodwill and Other, all assets and liabilities acquired in purchase acquisitions, including goodwill, indefinite-lived intangibles and other intangibles are recorded at fair value. We consider our accounting policies related to goodwill and other intangible assets to be critical because the assumptions or judgment used in determining the fair value of assets and liabilities acquired in past acquisitions are subjective and complex. As a result, changes in these assumptions or judgment could have a significant impact on our financial condition or results of operations.

The fair value of acquired assets and liabilities, including the resulting goodwill, was based either on quoted market prices or provided by other third-party sources, when available. When third-party information was not available we made good-faith estimates primarily through the use of internal cash flow modeling techniques. The assumptions used in the cash flow modeling are subjective and susceptible to significant changes.

Goodwill and other intangible assets with indefinite useful lives are tested for impairment at least annually and written down and charged to results of operations only in periods in which the recorded value is more than the estimated fair value. Intangible assets that have finite useful lives will continue to be amortized over their useful lives and are periodically evaluated for impairment. As of September 30, 2011, goodwill totaled \$28.1 million, the majority of which is in the WSFS Bank reporting unit and is the result of a multi-branch acquisition in 2008 and the acquisition of CB&T during 2010. In addition, and mainly as a result of the CB&T acquisition, amortizing intangibles totaled \$6.4 million as of September 30, 2011.

Goodwill was tested for impairment at December 31, 2010 using a two-step process that began with an estimation of fair value. The first step compared the estimated fair value of our reporting units with their carrying amounts, including goodwill. The estimated fair value exceeded its carrying amount; goodwill was not considered impaired. However, if the carrying amount exceeded its estimated fair value, a second step would be performed comparing the implied fair value to the carrying amount of goodwill. An impairment loss would be recorded to the extent that the carrying amount of goodwill exceeds its implied fair value.

Fair value may be determined using market prices, comparison to similar assets, market multiples, discounted cash flow analyses and other variables. Estimated cash flows extend five years into the future and, by their nature, are difficult to estimate over such an extended period of time. Factors that may significantly affect estimates include, but are not limited to, balance sheet growth assumptions, credit losses in our investment and loan portfolios, competitive pressures in our market area, changes in customer base and customer product preferences, changes in revenue growth trends, cost structure, changes in discount rates, conditions in the banking sector and general economic variables.

Goodwill and intangibles are also tested for impairment between annual tests if an event occurs or circumstances change that would cause a reduction in the fair value below its carrying value. As of December 31, 2010, we completed the Step One test of the analysis to determine potential goodwill impairment of the WSFS Bank reporting unit. The valuation incorporated a market-based analysis and indicated the fair value of our WSFS Bank reporting

unit was 43% above the carrying amount. Therefore, in accordance with FASB ASC 350-20-35-6, the Step Two analysis was not required.

At September 30, 2011, no events occurred that would cause a reduction in the fair value below its carrying value and therefore goodwill and other intangible assets were not considered impaired. Changing economic conditions that may adversely affect our performance and stock price could result in impairment, which could adversely affect earnings in the future.

FINANCIAL CONDITION, CAPITAL RESOURCES AND LIQUIDITY

Financial Condition

Our total assets increased \$235.0 million during the nine months ended September 30, 2011 to \$4.2 billion. Cash and cash equivalents increased \$86.8 million, or 23%, as a result of growth in our Cash Connect division. Mortgage-backed securities increased \$71.4 million or 10%. Loans increased \$74.1 million from December 31, 2010 mainly due to an increase in C&I loans which grew \$159.5 million, or 13%, as a result of our focus on franchise growth. This growth in commercial and industrial (C&I) loans was offset by intentional reductions of \$31.9 million in residential mortgage loans, \$29.2 million in construction loans balances, and a decrease in commercial real estate loans of \$18.1 million during 2011.

Our credit policy includes a “House Limit” to one borrowing relationship of \$25 million. The “House Limit” is restricted to a total of ten relationships and an aggregate exposure not to exceed 10% of our total Tier 1 capital plus our allowance for loan losses. Such exceptions are approved only in rare circumstances. Currently we have two relationships that exceed this limit and were approved because either the relationship contained several loans/borrowers that have no economic relationship (typically real estate investors with amounts diversified across a number of properties) or the exposure was marginally in excess of the “House Limit” and the credit profile was deemed strong.

Total liabilities increased \$215.8 million between December 31, 2010 and September 30, 2011 to \$3.8 billion. This increase was mainly due to savings deposits which increased \$120.2 million, or 47%. Interest-bearing and noninterest-bearing demand deposits increased \$70.4 million, or 9%. Jumbo certificates of deposit also increased \$26.9 million, or 9%. Time deposits decreased by \$41.9 million, or 9%. Federal Home Loan Bank advances increased \$79.8 million, or 16%, offset by other borrowed funds which decreased \$22.4 million, or 24%.

As we have continued to establish ourselves as a full service bank, and a premier bank in our markets, our level of public funding, trust and large commercial accounts has increased significantly. These account balances may add more seasonality and uneven trends to our deposit flows. As of September 30, 2011, our top ten depositors represented approximately 11% of our total customer funding.

Capital Resources

Stockholders’ equity increased \$19.4 million between December 31, 2010 and September 30, 2011. This increase was mainly due to net income of \$16.5 million as well as an increase of \$5.8 million in the value of our available-for-sale securities portfolio. Partially offsetting these increases was the payment of common and preferred dividends of \$5.1 million during the nine months ended September 30, 2011.

Book value per common share was \$44.97 at September 30, 2011 an increase of \$1.82 from \$43.15 reported at December 31, 2010. Tangible common book value per common share (a non-GAAP measurement) was \$34.88 at September 30, 2011, an increase of \$1.85, or 6% from \$33.03 reported at December 31, 2010.

Below is a table comparing the Bank’s consolidated capital position to the minimum regulatory requirements as of September 30, 2011:

Consolidated Bank Capital	For Capital Adequacy Purposes	To be Well-Capitalized Under Prompt Corrective Action Provisions
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(dollars in thousands)	Amount	% of Assets	Amount	% of Assets	Amount	% of Assets
Total Capital (to Risk-Weighted Assets)	\$426,868	13.52	% \$252,576	8.00	% \$315,720	10.00 %
Core Capital (to Adjusted Total Assets)	387,325	9.35	165,737	4.00	207,171	5.00
Tangible Capital (to Tangible Assets)	387,325	9.35	62,151	1.50	N/A	N/A
Tier 1 Capital (to Risk-Weighted Assets)	387,325	12.27	126,288	4.00	189,432	6.00

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Under guidelines issued by banking regulators, savings institutions such as the Bank must maintain “tangible” capital equal to 1.5% of adjusted total assets, “core” capital equal to 4.0% of adjusted total assets, “Tier 1” capital equal to 4.0% of risk weighted assets and “total” or “risk-based” capital (a combination of core and “supplementary” capital) equal to 8.0% of risk-weighted assets. Failure to meet minimum capital requirements can initiate certain mandatory actions and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on our bank’s financial statements.

At September 30, 2011, the Bank was in compliance with regulatory capital requirements and was considered a “well-capitalized” institution. The Bank’s core capital ratio of 9.35%, Tier 1 capital ratio of 12.27% and total risk based capital ratio of 13.52%, all remain substantially in excess of “well-capitalized” regulatory benchmarks, the highest regulatory capital rating. In addition, and not included in Bank capital, the holding company held \$13.3 million in cash to support dividends, acquisitions, strategic growth plans, and help fund the eventual repurchase of securities sold to the Treasury under the CPP Plan, which would require regulatory approval.

Recently Issued Guidance on Federal Debt

On August 5, 2011, Standard and Poor’s rating agency lowered the long-term rating of the U.S. government and federal agencies from AAA to AA+. In a joint press release issued by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration and the Office of the Comptroller of the Currency, the following guidance was provided related to the downgrade: for risk-based capital purposes, the risk weights for U.S. Treasury securities and other securities issued or guaranteed by the U.S. government, government agencies and government-sponsored entities will not change. In addition, the treatment of U.S. Treasury securities and other securities issued or guaranteed by the U.S. government, government agencies and government-sponsored entities will be unaffected.

Liquidity

We manage our liquidity risk and funding needs through our Treasury function and our Asset/Liability Committee. We have a policy that separately addresses liquidity, and management monitors our adherence to policy limits. Also, liquidity risk management is a primary area of examination by the banking regulators.

As a financial institution, the Bank has ready access to several sources to fund growth and meet its liquidity needs. Among these are: net income, retail deposit programs, loan repayments, borrowing from the FHLB, repurchase agreements, access to the Fed Discount Window, and access to the brokered deposit market as well as other wholesale funding avenues. In addition, we have a large portfolio of high-quality, liquid investments, primarily short-duration mortgage-backed securities and government sponsored enterprises (“GSE”) notes that provide a near-continuous source of cash flow to meet current cash needs, or can be sold to meet larger discrete needs for cash. Management believes these sources are sufficient to maintain the required and prudent levels of liquidity.

During the nine months ended September 30, 2011, cash and cash equivalents increased \$86.8 million to \$463.6 million. The increase was a result of the following: a \$147.1 million increase in cash provided through increases in demand, savings, and time deposits; \$79.8 million from FHLB advances; an increase of \$66.9 million from cash provided by our operating activities; and activity in investment securities of \$4.6 million. Offsetting these increases were cash usages of: a \$118.1 million net increase in loans; purchases of \$61.7 million in mortgage-backed securities available-for-sale net of repayments and sales; a \$28.2 million decrease in brokered deposits; investment in premises and equipment of \$8.1 million; and dividends paid of \$5.1 million.

NONPERFORMING ASSETS

The following table shows our nonperforming assets and past due loans at the dates indicated. Nonperforming assets include nonaccruing loans, nonperforming real estate, assets acquired through foreclosure and restructured mortgage and home equity consumer debt. Nonaccruing loans are those on which the accrual of interest has ceased. Loans are placed on nonaccrual status immediately if, in the opinion of management, collection is doubtful, or when principal or interest is past due 90 days or more and the value of the collateral is insufficient to cover principal and interest. Interest accrued but not collected at the date a loan is placed on nonaccrual status is reversed and charged against interest income. In addition, the amortization of net deferred loan fees is suspended when a loan is placed on nonaccrual status. Subsequent cash receipts are applied either to the outstanding principal balance or recorded as interest income, depending on management's assessment of the ultimate collectability of principal and interest. Past due loans are loans contractually past due 90 days or more as to principal or interest payments but which remain on accrual status because they are considered well secured and in the process of collection.

	September 30, 2011		December 31, 2010
	(In Thousands)		
Nonaccruing loans:			
Commercial	\$ 21,370		\$ 21,577
Consumer	1,562		3,701
Commercial mortgage	20,875		9,490
Residential mortgage	10,571		11,739
Construction	21,701		30,260
Total nonaccruing loans	76,079		76,767
Assets acquired through foreclosure	11,880		9,024
Troubled debt restructuring (accruing)	8,709		7,107
Total nonperforming assets	\$ 96,668		\$ 92,898
Past due loans(1):			
Residential Mortgages	562		465
Commercial and commercial mortgages	967		-
Total past due loans	\$ 1,529		\$ 465
Ratios:			
Allowance for loan losses to total loans (2)	1.97	%	2.30 %
Nonperforming assets to total assets	2.31	%	2.35 %
Nonaccruing loans to total loans (2)	2.82	%	2.93 %
Loan loss allowance to nonaccruing loans	69.91	%	78.60 %
Loan loss allowance to total nonperforming assets	55.02	%	64.95 %

(1) Past due loans are accruing loans which are contractually past due 90 days or more as to principal or interest. These loans are well secured and in the process of collection.

(2) Total loans exclude loans held for sale.

Nonperforming assets increased \$3.8 million between December 31, 2010 and September 30, 2011. Nonperforming loans decreased slightly during this period as the increase within the Commercial Mortgage portfolio has been more than offset by decreases within the Construction and Retail portfolios. Year to date, the migration of additional assets to Real Estate Owned (REO) have outpaced sales by \$2.9 million. A 23% net increase in accruing Troubled Debt Restructurings (TDR) accounts for the remainder of the increase.

The following table summarizes the changes in nonperforming assets during the period indicated:

	For the nine months ended September 30, 2011		For the year ended December 31, 2010
	(In Thousands)		
Beginning balance	\$ 92,898		\$ 82,160
Additions	75,524		89,876
Collections	(31,681)		(38,459)
Transfers to accrual	(7,386)		(1,077)

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Charge-offs / write-downs, net	(32,687)	(39,602)
Ending balance	\$ 96,668	\$ 92,898

The timely identification of problem loans is a key element in our strategy to manage our loan portfolio. Timely identification enables us to take appropriate action and, accordingly, minimize losses. An asset review system established to monitor the asset quality of our loans and investments in real estate portfolios facilitates the identification of problem assets. In general, this system utilizes guidelines established by federal regulation.

INTEREST SENSITIVITY

The matching of maturities or repricing periods of interest rate-sensitive assets and liabilities to promote a favorable interest rate spread and mitigate exposure to fluctuations in interest rates is our primary tool for achieving our asset/liability management strategies. We regularly review our interest-rate sensitivity and adjust the sensitivity within acceptable tolerance ranges established by the Board of Directors. At September 30, 2011, interest-earning assets exceeded interest-bearing liabilities that mature or reprice within one year (interest-sensitive gap) by \$99.4 million. Our interest-sensitive assets as a percentage of interest-sensitive liabilities within the one-year window decreased from 106.0% at June 30, 2011, to 104.4% at September 30, 2011. Likewise, the one-year interest-sensitive gap as a percentage of total assets changed to 2.4% at September 30, 2011 from 3.2% at June 30, 2011. The change in sensitivity since June 30, 2011 reflects the current interest rate environment and our continuing effort to effectively manage interest rate risk.

Market risk is the risk of loss from adverse changes in market prices and rates. Our market risk arises primarily from interest rate risk inherent in our lending, investing, and funding activities. To that end, we actively monitor and manage our interest rate risk exposure. One measure, required to be performed by federal regulation, measures the impact of an immediate change in interest rates in 100 basis point increments on the net portfolio value ratio. The net portfolio value ratio is defined as the net present value of the estimated cash flows from assets and liabilities as a percentage of net present value of cash flows from total assets (or the net present value of equity). The table below shows the estimated impact of immediate changes in interest rates on our net interest margin and net portfolio value ratio at the specified levels at September 30, 2011 and 2010:

Change in Interest Rate (Basis Points)	2011		2010	
	% Change in Net Interest Margin (1)	Net Portfolio Value (2)	% Change in Net Interest Margin (1)	Net Portfolio Value (2)
+300	7%	10.98%	8%	10.72%
+200	4%	11.10%	5%	11.04%
+100	0%	11.22%	3%	11.02%
-	0%	11.26%	0%	11.02%
-100	3%	11.00%	-9%	10.51%
-200 (3)	NMF	NMF	NMF	NMF
-300 (3)	NMF	NMF	NMF	NMF

- (1) The percentage difference between net interest margin in a stable interest rate environment and net interest margin as projected under the various rate change environments.
- (2) The net portfolio value ratio of the Company in a stable interest rate environment and the net portfolio value ratio as projected under the various rate change environments.
- (3) Sensitivity indicated by a decrease of 200 or 300 basis points is not deemed meaningful at September 30, 2011 given the low absolute level of interest rates at that time.

We also engage in other business activities that are sensitive to changes in interest rates. For example, mortgage banking revenues and expenses can fluctuate with changing interest rates. These fluctuations are difficult to model and estimate.

COMPARISON OF THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2011 AND 2010

Results of Operations

We recorded net income of \$6.8 million or \$0.70 per diluted common share for the third quarter of 2011. This compares to net income of \$8.2 million or \$0.94 per diluted common share in the third quarter of 2010. The third quarter of 2010 results included a non-routine fraud loss recovery of \$4.5 million (pre-tax), or \$0.38 per diluted common share (after-tax) included in noninterest expenses. Earnings for the third quarter of 2011 were impacted by a reduction in loan loss provision of \$3.4 million to \$6.6 million when compared to the third quarter of 2010 and an increase of \$2.0 million in

fiduciary and investment management income. Excluding the previously mentioned fraud loss recovery, noninterest expense increased \$5.8 million as a result of a \$3.1 million increase in compensation expenses due to normal operating expenses for the Christiana Trust Division as well as franchise growth.

Net income for the first nine months of 2011 was \$16.5 million or \$1.66 per diluted common share. This is an increase of \$4.5 million when compared to net income of \$12.0 million or \$1.33 per diluted common share for the nine months ended September 30, 2010. Earnings for the first nine months of 2011 were impacted by a lower provision for loan losses which decreased \$10.9 million to \$21.0 million during the nine months ended September 30, 2011. In addition, fiduciary and investment management income increased \$5.7 million due to the addition of the Christiana Trust division in December of 2010. Finally, bank-owned life insurance income increased \$1.2 million as a result of unanticipated non-taxable income recorded during 2011. Partially offsetting these favorable items was an increase of \$15.0 million in noninterest expenses during the nine months ended September 30, 2011. This increase was due to the normal operating expenses from Christiana Trust as well as overall franchise growth including the addition of five new branches, the relocation of four branches and the addition of twelve commercial relationship managers and related support staff. Finally, during 2011 marketing expenses included an additional \$961,000 for our new "Right Here" marketing campaign.

Net Interest Income

The following tables provide information concerning the balances, yields and rates on interest-earning assets and interest-bearing liabilities during the periods indicated.

	Three Months Ended September 30,					
	2011			2010		
	Average Balance	Interest	Yield/ Rate (1)	Average Balance	Interest	Yield/ Rate (1)
(Dollars In Thousands)						
Assets:						
Interest-earning assets:						
Loans (2) (3):						
Commercial real estate loans	\$ 731,527	\$ 8,556	4.68 %	\$ 733,562	\$ 8,587	4.68 %
Residential real estate loans	293,800	3,454	4.70	341,033	4,275	5.01
Commercial loans	1,368,703	17,193	4.99	1,176,232	15,236	5.16
Consumer loans	296,709	3,737	5.00	290,346	3,566	4.87
Total loans	2,690,739	32,940	4.94	2,541,173	31,664	5.03
Mortgage-backed securities (4)	801,446	7,052	3.52	743,832	8,699	4.68
Investment securities (4) (5)	43,959	99	0.90	47,173	216	1.83
Other interest-earning assets	37,830	-	-	39,920	-	-
Total interest-earning assets	3,573,974	40,091	4.52	3,372,098	40,579	4.85
Allowance for loan losses	(57,125)			(64,428)		
Cash and due from banks	65,997			57,328		
Cash in non-owned ATMs	378,651			269,529		
Bank-owned life insurance	63,463			60,732		
Other noninterest-earning assets	119,888			98,863		
Total assets	\$ 4,144,848			\$ 3,794,122		
Liabilities and Stockholders' Equity:						
Interest-bearing liabilities:						
Interest-bearing deposits:						
Interest-bearing demand	\$ 324,367	\$ 75	0.09 %	\$ 263,428	\$ 102	0.15 %
Money market	731,979	720	0.39	628,124	1,016	0.64
Savings	375,243	386	0.41	242,831	127	0.21
Customer time deposits	757,975	3,237	1.69	772,900	3,906	2.00
Total interest-bearing customer deposits	2,189,564	4,418	0.80	1,907,283	5,151	1.07
	209,629	201	0.38	295,948	439	0.59

Brokered certificates of deposit						
Total interest-bearing deposits	2,399,193	4,619	0.76	2,203,231	5,590	1.01
FHLB of Pittsburgh advances	610,253	2,484	1.99	515,259	3,818	2.90
Trust preferred borrowings	67,011	340	1.59	67,011	370	2.16
Other borrowed funds	142,725	468	1.31	187,124	624	1.33
Total interest-bearing liabilities	3,219,182	7,911	0.98	2,972,625	10,402	1.40
Noninterest-bearing demand deposits	516,257			446,741		
Other noninterest-bearing liabilities	26,001			26,698		
Stockholders' equity	383,408			348,058		
Total liabilities and stockholders' equity	\$ 4,144,848			\$ 3,794,122		
Excess of interest-earning assets over interest-bearing liabilities	\$ 354,792			\$ 399,473		
Net interest and dividend income		\$ 32,180			\$ 30,177	
Interest rate spread			3.54 %			3.45 %
Net interest margin			3.63 %			3.61 %

(1) Weighted average yields have been computed on a tax-equivalent basis using a 35% effective tax rate.

(2) Nonperforming loans are included in average balance computations.

(3) Balances are reflected net of unearned income.

(4) Includes securities available-for-sale.

(5) Includes reverse mortgages.

	Nine Months Ended September 30,					
	2011			2010		
	Average Balance	Interest	Yield/ Rate (1)	Average Balance	Interest	Yield/ Rate (1)
(Dollars In Thousands)						
Assets:						
Interest-earning assets:						
Loans (2) (3):						
Commercial real estate loans	\$ 749,318	\$ 26,434	4.70 %	\$ 738,018	\$ 26,080	4.71 %
Residential real estate loans	303,371	11,009	4.84	347,630	13,268	5.09
Commercial loans	1,311,390	48,855	4.99	1,148,095	44,357	5.19
Consumer loans	302,732	11,401	5.04	294,846	10,792	4.89
Total loans	2,666,811	97,699	4.93	2,528,589	94,497	5.03
Mortgage-backed securities (4)	749,961	20,962	3.73	743,903	27,370	4.91
Investment securities (4) (5)	43,164	396	1.22	45,830	718	2.09
Other interest-earning assets	36,990	-	-	39,916	6	0.02
Total interest-earning assets	3,496,926	119,057	4.57	3,358,238	122,591	4.90
Allowance for loan losses	(58,435)			(60,276)		
Cash and due from banks	62,869			59,877		
Cash in non-owned ATMs	342,345			257,483		
Bank-owned life insurance	64,221			60,529		
Other noninterest-earning assets	120,583			109,528		
Total assets	\$ 4,028,509			\$ 3,785,379		
Liabilities and Stockholders' Equity:						
Interest-bearing liabilities:						
Interest-bearing deposits:						
Interest-bearing demand	\$ 316,712	\$ 301	0.13 %	\$ 259,106	\$ 321	0.17 %
Money market	712,404	2,293	0.43	606,722	3,311	0.73
Savings	348,967	1,215	0.47	238,345	362	0.20
Customer time deposits	769,528	10,491	1.82	756,283	12,164	2.14
Total interest-bearing customer deposits	2,147,611	14,300	0.89	1,860,456	16,158	1.16
Brokered certificates of deposit	190,395	576	0.40	320,666	1,497	0.62

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Total interest-bearing deposits	2,338,006	14,876	0.85	2,181,122	17,655	1.08
FHLB of Pittsburgh advances	558,807	7,866	1.86	575,186	11,812	2.71
Trust preferred borrowings	67,011	1,015	2.00	67,011	1,047	2.06
Other borrowed funds	158,822	1,679	1.41	180,197	1,859	1.38
Total interest-bearing liabilities	3,122,646	25,436	1.09	3,003,516	32,373	1.44
Noninterest-bearing demand deposits	506,316			432,693		
Other noninterest-bearing liabilities	22,744			26,117		
Stockholders' equity	376,803			323,053		
Total liabilities and stockholders' equity	\$ 4,028,509			\$ 3,785,379		
Excess of interest-earning assets over interest-bearing liabilities	\$ 374,280			\$ 354,722		
Net interest income		\$ 93,621			\$ 90,218	
Interest rate spread			3.48 %			3.46 %
Net interest margin			3.60 %			3.61 %

(1) Weighted average yields have been computed on a tax-equivalent basis using a 35% effective tax rate.

(2) Nonperforming loans are included in average balance computations.

(3) Balances are reflected net of unearned income.

(4) Includes securities available-for-sale.

(5) Includes reverse mortgages.

Net interest income for the third quarter of 2011 improved by \$2.0 million, or 7%, compared to the third quarter of 2010. The increase in net interest income reflects an improvement in the loan mix as well as effective management of funding costs, both deposit pricing and wholesale funding rates.

The net interest margin for the third quarter of 2011 was 3.63%, a two basis point increase compared to 3.61% for the third quarter of 2010. This was the result of our ability to decrease funding costs in nearly all categories, most notably FHLB advances. Rates on FHLB advances dropped significantly from the third quarter of 2010.

Net interest income for the nine months ended September 30, 2011 was \$93.6 million compared to \$90.2 million for the same period in 2010. Consistent with the quarterly trend discussed above, the increase in net interest income was a result of the loan mix improvement as well as effective management of funding costs, both deposit pricing and wholesale funding rates.

Allowance for Loan Losses

We maintain allowances for loan losses and charge losses to these allowances when such losses are identified. The determination of the allowance for loan losses requires significant judgment reflecting our best estimate of probable loan losses related to specifically identified loans as well as probable loan losses in the remaining loan portfolio. Our evaluation is based upon a continuing review of these portfolios.

We established our loan loss allowance in accordance with guidance provided in the Securities and Exchange Commission's Staff Accounting Bulletin 102 ("SAB 102"). Its methodology for assessing the appropriateness of the allowance consists of several key elements which include: specific allowances for identified problem loans; formula allowances for commercial and commercial real estate loans; and allowances for pooled homogenous loans.

Specific reserves are established for certain impaired loans in cases where we have identified significant conditions or circumstances related to a specific credit that indicate the probability that a loss has been incurred.

The formula allowances for commercial and commercial real estate loans are calculated by applying estimated loss factors to outstanding loans based on the internal risk grade of loans. For lower risk commercial and commercial real estate loans the portfolio is pooled and based on internal risk grade only. Higher risk and criticized loans have loss factors that are derived from an analysis of both the probability of default and the loss given default should default occur. Loss adjustment factors are applied based on criteria discussed below. As a result, changes in risk grades of both performing and nonperforming loans affect the amount of the formula allowance.

Pooled loans are usually smaller, not-individually-graded and homogenous in nature, such as consumer installment loans and residential mortgages. Loan loss allowances for pooled loans are first based on a ten-year net charge-off history. The average loss allowance per homogenous pool is based on the product of average annual historical loss rate and the homogeneous pool balances. These separate risk pools are then assigned a reserve for losses based upon this historical loss information and loss adjustment factors.

Historical loss adjustment factors are based upon our evaluation of various current conditions, including those listed below.

- General economic and business conditions affecting the Bank's key lending areas,
 - Credit quality trends,
 - Recent loss experience in particular segments of the portfolio,
 - Collateral values and loan-to-value ratios,
 - Loan volumes and concentrations, including changes in mix,
 - Seasoning of the loan portfolio,
 - Specific industry conditions within portfolio segments,
 - Bank regulatory examination results, and
- Other factors, including changes in quality of the loan origination, servicing and risk management processes.

Our loan officers and risk managers meet at least quarterly to discuss and review these conditions and risks associated with individual problem loans. In addition, various regulatory agencies, independent auditors and loan review consultants periodically review our loan ratings and allowance for loan losses.

During the third quarter of 2011, the provision for loan losses was impacted by a higher level of estimated losses related to consumer loans using updated historical data as adjusted for the current periods charge-offs and trends. The annual third quarter adjustment was consistent with the prior year and resulted in an increase of approximately \$1.7 million, net, from the estimate previously used.

The provision for loan losses was \$6.6 million in the quarter ending September 30, 2011 compared to \$10.0 million in the same quarter of 2010. Total credit costs (including the provision for loan losses, loan workout expense, OREO expense and letter of credit reserve) improved to \$8.4 million from \$10.2 million in the second quarter of 2011 and \$10.9 million in the third quarter last year. The provision for loan losses for the nine months ending September 30, 2011 was \$21.0 million compared to \$32.0 million for the nine months ending September 30, 2010.

The table below represents a summary of the changes in the allowance for loan losses during the periods indicated.

	For the Nine Months Ended September 30,				
	2011		2010		
	(Dollars in Thousands)				
Beginning balance	\$	60,339	\$	53,446	
Provision for loan losses		21,048		31,980	
Charge-offs:					
Residential real estate		2,183		1,580	
Commercial real estate		6,609		3,083	
Construction		8,179		5,231	
Commercial		7,641		7,820	
Overdrafts		613		726	
Consumer		4,859		4,231	
Total charge-offs		30,084		22,671	
Recoveries:					
Residential real estate		116		19	
Commercial real estate		381		68	
Construction		557		950	
Commercial (2)		409		288	
Overdrafts		267		290	
Consumer		155		108	
Total recoveries		1,885		1,723	
Net charge-offs		28,199		20,948	
Ending balance	\$	53,188	\$	64,478	
Net charge-offs to average gross loans outstanding, net of unearned income (1)		1.41	%	1.11	%

(1) Ratios for the nine months ended September 30, 2011 and September 30, 2010 are annualized

(2) Commercial recoveries include a one-time adjustment for the reclassification of an unfunded commitment reserve previously included in the allowance for loan loss to a liability reserve account.

Noninterest Income

Noninterest income increased \$2.5 million to \$16.9 million for the quarter ended September 30, 2011 compared to \$14.4 million in the third quarter of 2010. Excluding the impact of net securities gains in both periods, noninterest income

increased by \$2.3 million, or 18%. Noninterest income for the third quarter of 2011 increased \$2.0 million in fiduciary and investment management income resulting primarily from the December 2010 acquisition of CB&T. In addition, increases in credit/debit card and ATM fees and deposit service charges more than offset declines in mortgage banking revenues and the negative impact of new banking regulations (Reg E) that went into effect during the third quarter of 2010.

For the nine months ended September 30, 2011, noninterest income increased \$8.6 million to \$46.6 million, from \$38.0 million in the same period of 2010. Excluding the impact from net securities gains from both periods and \$1.2 million in unanticipated BOLI income recorded in the second quarter of 2011, noninterest income increased \$6.5 million. This increase was mainly due to a \$5.7 million increase in fiduciary and investment management income resulting from the acquisition of CB&T and a \$1.4 million increase in credit/debit card and ATM fees due to franchise growth. These increases were partially offset by a decrease of \$406,000 in deposit service charges due to the impact of the new banking regulations (Reg E) during the third quarter of 2010.

Noninterest Expense

Noninterest expense increased \$10.3 million to \$32.4 million in the third quarter of 2011 compared to \$22.1 million in the same period in 2010. The third quarter of 2011 included an additional \$961,000 of marketing expense from the Company's "Right Here" marketing campaign. Excluding the marketing campaign, as well as the fraud recovery and CB&T integration costs included in the third quarter of 2010, noninterest expenses increased \$5.0 million, or 19%, over the third quarter of 2010. This increase was mainly due to increased compensation, occupancy, equipment, data processing and operations expenses as a result of our accelerated franchise growth. Included in this growth are normal operating expenses for the Christiana Trust division acquired in December 2010. Also adding to the variance was a \$956,000 increase in 2011 loan workout and OREO expense.

For the nine months ended September 30, 2011, noninterest expense increased \$15.0 million to \$94.5 million, compared to \$79.5 million in the same period in 2010. Similar to the quarterly comparison, the main reasons for this increase were the related costs of our accelerated growth, the additional marketing expense of \$961,000 and the non-routine expenses related to the integration of Christiana Trust totaling \$780,000. Related growth expenses for the nine months ended September 30, 2011, included the opening of five new branches, relocating four new branches and hiring 12 new commercial relationship managers and related staff during the past year.

Income Taxes

We and our subsidiaries file a consolidated Federal income tax return and separate state income tax returns. Income taxes are accounted for in accordance with ASC 740, which requires the recording of deferred income taxes for tax consequences of temporary differences. We recorded an income tax expense of \$3.3 million and \$8.2 million during the three and nine months ended September 30, 2011, respectively, compared to an income tax expense of \$4.3 million and \$4.7 million for the same periods in 2010. The second quarter of 2011 included the recognition of tax benefits related to \$1.2 million of tax-free income from life insurance proceeds received from our bank owned life insurance investment. The third quarter of 2011 included tax benefits of \$376,000 resulting primarily from a decrease in our income tax reserve due to the expiration of the statute of limitations on certain items. The first quarter of 2010 included a tax benefit of \$899,000 resulting from a decrease in our income tax reserve due to the expiration of the statute of limitations on certain tax items. Our effective tax rate was 33.0% and 33.2% for the three and nine months ended September 30, 2011 compared to 34.4% and 28.2% during the same periods in 2010. Excluding the tax-free BOLI proceeds and statute of limitations related benefit, our effective tax rates were 36.7% and 36.3% for the three and nine months ended September 30, 2011 compared to 34.4% and 33.6% during the same periods in 2010.

The effective tax rate reflects the recognition of certain tax benefits in the financial statements including those benefits from tax-exempt interest income (including a 50% interest income exclusion on a loan to an Employee Stock Ownership Plan) and BOLI income. These tax benefits are offset by the tax effect of stock-based compensation expense related to incentive stock options and a provision for state income tax expense.

We frequently analyze our projections of taxable income and make adjustments to our provision for income taxes accordingly.

RECENT ACCOUNTING PRONOUNCEMENTS

In January 2010, the FASB issued an update (Accounting Standards Update No. 2010-06, Improving Disclosures about Fair Value Measurements) impacting FASB ASC 820, Fair Value Measurements and Disclosures. The update provides clarification regarding existing disclosures and requires additional disclosures regarding fair value measurements. Specifically, the guidance now requires reporting entities to disclose the amounts of significant transfers between levels and the reasons for the transfers. In addition, the reconciliation should present separate information about purchases, sales, issuances and settlements. A reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value. The new standard was effective for reporting periods beginning after December 15, 2009 except for disclosures about purchases, sales, issuances and settlements which were not effective until reporting periods beginning after December 15, 2010. There was no transfer into or out of Level 1 or Level 2 of the fair value hierarchy in the first nine months of 2011. Adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

In July 2010, the FASB issued an update (Accounting Standards update No. 2010-20, Receivables, Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses) This update improves the disclosures that an entity provides about the credit quality of its financing receivables and the related allowance for credit losses. As a result of these amendments, an entity is required to disaggregate, by portfolio segment or class, certain existing disclosures, and to provide certain new disclosures about its financing receivables and related allowances for credit losses. The disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The amendment does not require comparative disclosures for earlier reporting periods that ended before adoption, however, an entity should provide comparative disclosures for those reporting periods after initial adoption. The adoption of this amendment did not have a material effect on our Consolidated Financial Statements.

In April 2011, the FASB issued an update (Accounting Standards update No. 2011-02, A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring) which clarifies when creditors should classify loan modifications as troubled debt restructurings. The new guidance is effective for interim and annual periods beginning on or after June 15, 2011, and applies retrospectively to restructurings occurring on or after January 1, 2011. A provision in Update 2011-02 also ends the FASB's deferral of the additional disclosures about troubled debt restructurings as required by Update 2010-20. The adoption of this amendment did not have a material effect on our Consolidated Financial Statements.

In April 2011, the FASB issued an update (Accounting Standards Update No. 2011-03, Reconsideration of Effective Control in Repurchase Agreements) which removes from the assessment of effective control the criterion related to the transferor's ability to repurchase or redeem financial assets on substantially agreed terms, even in the event of default by the transferee. In addition, this guidance also eliminates the requirement to demonstrate that a transferor possesses adequate collateral to fund substantially all the cost of purchasing replacement financial assets. The new guidance is effective for interim and annual periods beginning on or after December 15, 2011, and applies prospectively to transactions or modifications of existing transactions occurring on or after the effective date. We are still evaluating if the adoption of this guidance will have a material impact on our Consolidated Financial Statements.

In May 2011, the FASB issued an update (Accounting Standards Update No. 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS) to achieve common fair value measurement and disclosure requirements between U.S. and International accounting principles. While the overall guidance is consistent with U.S. GAAP, the amendment includes additional fair value disclosure requirements. The amendments in the guidance are effective for interim and annual periods beginning after December 15, 2011. We are still evaluating if the adoption of this guidance and additional disclosures will have a material

impact on our Consolidated Financial Statements.

In June 2011, the FASB issued an update (Accounting Standards Update No. 2011-05, Presentation of Comprehensive Income) to eliminate the option to present the components of other comprehensive income as part of the statement of changes in shareholder's equity. The amendment requires that comprehensive income be presented in either a single continuous statement or in two separate consecutive statements. This amendment is effective for interim and annual periods beginning after December 15, 2011. We do not expect the adoption of this guidance to have a material impact on our financial statements.

In September 2011, the FASB issued an update (Accounting Standards Update No. 2011-08, Intangibles - Goodwill and Other (Topic 350) - Testing Goodwill for Impairment) to give entities the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity

determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. However, if an entity concludes otherwise, then it is required to perform the first step of the two-step impairment test by calculating the fair value of the reporting unit and comparing the fair value with the carrying amount of the reporting unit. This amendment is effective for interim and annual periods beginning after December 15, 2011. We do not expect the adoption of this guidance to have a material impact on our financial statements.

RECENT LEGISLATION

On July 21, 2010, the President signed the Dodd-Frank Act into law. This legislation makes extensive changes to the laws regulating financial services firms and requires significant rule-making. In addition, the legislation mandates multiple studies, which could result in additional legislative or regulatory action. While the full effects of the legislation on us cannot yet be determined, this legislation was opposed by the American Bankers Association and is generally perceived as negatively impacting the banking industry. This legislation may result in higher compliance and other costs, reduced revenues and higher capital and liquidity requirements, among other things, which could adversely affect our business. There are many parts of the Dodd-Frank Act that have yet to be determined and implemented; however, as a direct result of the Act, the following rulings have been adopted or will be adopted in the coming years:

- On August 10, 2010 the Board of Directors of the FDIC adopted a final ruling permanently increasing the standard maximum deposit insurance amount from \$100,000 to \$250,000, which became effective on July 22, 2010.
- During January 2011, a timeline and preliminary implementation plan for the phase out of The Office of Thrift Supervision (“the OTS”), and its merger into the Office of the Comptroller of the Currency was announced by the joint agencies. One of the provisions of the plan include a transition from the Thrift Financial Report, which we file each quarter, to the Call Report, expected to begin with the March 2012 reporting period.
- On February 7, 2011, the Federal Reserve approved a final ruling that changes the Deposit Insurance Fund (“DIF”) assessment from domestic deposits to average assets minus tangible equity. The changes went into effect during the second quarter of 2011.
- On June 29, 2011 the Federal Reserve issued its final debit card interchange rule, establishing a debit card interchange fee cap. The rule was effective October 1, 2011 and applies to issuers that, together with their affiliates, have assets of \$10 billion or more. The final ruling caps issuers base fee at 21 cents per transaction and allows for a 5 basis-point charge per transaction to help cover fraud loss.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Incorporated herein by reference from Item 2, of this quarterly report on Form 10-Q.

Item 4. Controls and Procedures

- (a) Evaluation of disclosure controls and procedures. Based on their evaluation of our disclosure controls and procedures (as defined in Rules 13a-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”)), our principal executive officer and the principal financial officer have concluded that as of the end of the period covered by this Quarterly Report on Form 10-Q such disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities and Exchange Commission’s rules and forms and is accumulated and communicated to our management, including the principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding

required disclosures.

(b) Changes in internal control over financial reporting. During the quarter under report, there was no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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Part II. OTHER INFORMATION

Item 1. Legal Proceedings

Incorporated herein by reference to Note 16 – Legal Proceedings to the Consolidated Financial Statements

Item 1A. Risk Factors

Our management does not believe there have been any material changes to the risk factors previously disclosed under Item 1A. of the Company's Form 10-K for the year ended December 31, 2010, previously filed with the Securities and Exchange Commission.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table represents information with respect to repurchases of common stock made by us during the three months ended September 30, 2011. These shares were delivered to us by employees as payment for taxes on the vesting of restricted stock or exercise of stock options.

2011	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicity Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
July	-	\$ -	-	-
August	-	-	-	-
September	1,494	34.00	-	-
Total (1)	1,494	\$ 34.00	-	-

(1) The shares repurchased were not part of a publicly announced repurchase plan or program. These shares were owned and tendered by employees as payment for taxes on vesting of restricted stock or exercise of stock options. There were no treasury shares repurchased during the quarter ended September 30, 2011.

Item 3. Defaults upon Senior Securities

Not applicable

Item 4. [Reserved]

Not applicable

Item 5. Other Information

Not applicable

Item 6. Exhibits

- (a) Exhibit 31.1 – Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- (b) Exhibit 31.2 – Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- (c) Exhibit 32 – Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- (d) Exhibit 101.INS – XBRL Instance Document *
- (e) Exhibit 101.SCH – XBRL Schema Document*
- (f) Exhibit 101.CAL – XBRL Calculation Linkbase Document*
- (g) Exhibit 101.LAB – XBRL Labels Linkbase Document*
- (h) Exhibit 101.PRE – XBRL Presentation Linkbase Document*
- (i) Exhibit 101.DEF – XBRL Definition Linkbase Document*

* Pursuant to Regulation 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Section 11 or 12 of the Securities Act of 1933, as amended, or Section 18 of the Securities Exchange Act of 1934, as amended, and are otherwise not subject to liability.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

WSFS FINANCIAL CORPORATION

Date: November 9,
2011

/s/ Mark A. Turner

Mark A. Turner
President and Chief Executive Officer

Date: November 9,
2011

/s/ Stephen A. Fowle

Stephen A. Fowle
Executive Vice President and
Chief Financial Officer