RingCentral Inc
Form 10-Q
November 03, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2014

OR

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

For the transition period from to

Commission File Number: 001-36089

RingCentral, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware	94-3322844
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1400 Fashion Island Boulevard, Suite 700

San Mateo, California 94404

(Address of principal executive offices)

(650) 472-4100

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See 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 x (do not check if a smaller reporting company)	Smaller reporting company ¨

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

As of October 28, 2014, there were 49,769,673 shares of Class A Common Stock issued and outstanding and 18,344,298 shares of Class B Common Stock outstanding.

TABLE OF CONTENTS

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements that are based on our management's beliefs and assumptions and on information currently available to our management. The forward-looking statements are contained principally in, but not limited to, the sections titled "Risk Factors," and "Management's Discussion and Analysis of Financial Condition and Results of Operations." Forward-looking statements include all statements that are not historical facts and can be identified by terms such as "anticipates," "believes," "could," "seeks," "estimates," "expects," "intends," "may," "plans," "potential," "predicts", "projects," "should," "will," "would" or similar expressions and the negative terms. Forward-looking statements include, but are not limited to, statements about:

- our future financial performance;
- our anticipated growth and growth strategies and our ability to effectively manage that growth and effect these strategies;
- anticipated trends, developments and challenges in our business and in the markets in which we operate;
- our ability to anticipate and adapt to future changes in our industry;
- our ability to anticipate market needs and develop new and enhanced products and services to meet those needs, and our ability to successfully monetize them;
- maintaining and expanding our customer base;
- maintaining, expanding and responding to changes in our relationships with other companies;
- the impact of competition in our industry and innovation by our competitors;
- our ability to sell our products;
- our ability to expand our business to larger customers and internationally;
- the impact of seasonality on our business;
- the impact of any failure of our solutions or solution innovations;
- our reliance on our third-party service providers;
- the potential effect on our business of litigation to which we may become a party;
- our liquidity and working capital requirements;
- the estimates and estimate methodologies used in preparing our consolidated financial statements; and
- the political environment and stability in the regions in which we or our subcontractors operate.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. We discuss these risks in greater detail in the section entitled "Risk Factors" and elsewhere in this Quarterly Report on Form 10-Q. Given these uncertainties, you should not place undue reliance on these forward-looking statements. Also, forward-looking statements represent our management's beliefs and assumptions only as of the date of this Quarterly Report on Form 10-Q. You should read this Quarterly Report on Form 10-Q completely and with the understanding that our actual future results may be materially different from what we expect.

Except as required by law, we assume no obligation to update these forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in these forward looking statements, even if new information becomes available in the future.

PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

RINGCENTRAL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited, in thousands)

	September 30, 2014	December 31, 2013
Assets:		
Current assets:		
Cash and cash equivalents	$120,691	$116,378
Short-term investments	28,662	—
Accounts receivable, net	7,443	3,045
Inventory	2,012	2,111
Prepaid expenses and other current assets	8,369	5,214
Total current assets	167,177	126,748
Property and equipment, net	25,862	16,660
Other assets	2,866	1,777
Total assets	$195,905	$145,185
Liabilities and Stockholders' Equity:		
Current liabilities:		
Accounts payable	$5,700	$4,414
Accrued liabilities	31,659	20,559
Current portion of capital lease obligation	615	347
Current portion of long-term debt	18,489	9,871
Deferred revenue	23,415	16,552
Total current liabilities	79,878	51,743
Long-term debt	8,750	24,356
Sales tax liability	3,953	3,988
Capital lease obligation	618	247
Other long-term liabilities	2,771	1,336
Total liabilities	95,970	81,670
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Common stock	7	6
Additional paid-in capital	268,189	193,574
Accumulated other comprehensive loss	(286)	(310)
Accumulated deficit	(167,975)	(129,755)

Total stockholders' equity	99,935	63,515
Total liabilities and stockholders' equity	$195,905	$145,185

See accompanying notes to condensed consolidated financial statements

RINGCENTRAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited, in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenues:				
Services	$51,951	$37,925	$143,668	$104,669
Product	4,993	4,009	14,325	10,494
Total revenues	56,944	41,934	157,993	115,163
Cost of revenues:				
Services	14,799	12,080	43,305	34,178
Product	4,606	3,888	13,546	10,189
Total cost of revenues	19,405	15,968	56,851	44,367
Gross profit	37,539	25,966	101,142	70,796
Operating expenses:				
Research and development	11,931	8,150	32,478	24,260
Sales and marketing	26,697	18,889	76,342	52,355
General and administrative	9,725	7,078	28,184	24,859
Total operating expenses	48,353	34,117	137,004	101,474
Loss from operations	(10,814)	(8,151)	(35,862)	(30,678)
Other income (expense), net:				
Interest expense	(505)	(995)	(1,582)	(2,222)
Other income (expense), net	(648)	348	(592)	102
Other income (expense), net	(1,153)	(647)	(2,174)	(2,120)
Loss before provision (benefit) for income taxes	(11,967)	(8,798)	(38,036)	(32,798)
Provision (benefit) for income taxes	19	54	184	(66)
Net loss	$(11,986)	$(8,852)	$(38,220)	$(32,732)
Net loss per common share:				
Basic and diluted	$(0.18)	$(0.36)	$(0.58)	$(1.41)
Weighted-average number of shares used in computing net loss per share:				
Basic and diluted	67,800	24,452	66,313	23,290

See accompanying notes to condensed consolidated financial statements

RINGCENTRAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Unaudited, in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net loss	$(11,986)	$(8,852)	$(38,220)	$(32,732)
Other comprehensive loss:				
Foreign currency translation adjustments, net	387	(313)	57	(69)
Unrealized loss on available-for-sale securities	(34)	-	(34)	-
Comprehensive loss	$(11,633)	$(9,165)	$(38,197)	$(32,801)

See accompanying notes to condensed consolidated financial statements

RINGCENTRAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited, in thousands)

	Nine Months Ended September 30,	
	2014	2013
Cash flows from operating activities:		
Net loss	$(38,220)	$(32,732)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	7,409	6,606
Share-based compensation	11,306	4,546
Noncash interest expense related to debt	194	412
Loss on disposal of assets	24	—
Deferred income tax	82	(45)
Changes in assets and liabilities:		
Accounts receivable	(4,398)	198
Inventory	100	(1,202)
Prepaid expenses and other current assets	(3,155)	(4,340)
Other assets	(1,109)	(155)
Accounts payable	1,078	1,652
Accrued liabilities	11,318	(366)
Deferred revenue	6,863	4,283
Other liabilities	1,400	553
Net cash used in operating activities	(7,108)	(20,590)
Cash flows from investing activities:		
Purchases of property and equipment	(15,169)	(9,024)
Purchases of available-for-sale securities	(28,696)	—
Restricted investments	—	(130)
Net cash used in investing activities	(43,865)	(9,154)
Cash flows from financing activities:		
Net proceeds from secondary public offering of common stock	57,167	—
Net proceeds from debt agreements	—	22,907
Repayment of debt	(7,182)	(5,928)
Repayment of capital lease obligations	(509)	(312)
Proceeds from issuance of preferred stock warrants	—	1,625
Payment of offering costs	(1,219)	(1,773)
Proceeds from issuance of stock in connection with stock plans	7,010	835
Net cash provided by financing activities	55,267	17,354
Effect of exchange rate changes on cash and cash equivalents	19	(22)
Net increase (decrease) in cash and cash equivalents	4,313	(12,412)
Cash and cash equivalents:		
Beginning of period	116,378	37,864
End of period	$120,691	$25,452
Supplemental disclosure of cash flow data:		
Cash paid for interest	$956	$1,187
Cash paid for income taxes	82	31

Noncash investing and financing activities:		
Change in liability for unvested exercised options	$37	$95
Issuance of common stock in connection with legal settlement	—	257
Accrued liability for deferred offering costs	—	2,135
Conversion of convertible preferred stock into common stock	—	74,020
Reclassification of preferred stock warrants from liability to equity	—	820
Equipment purchased and unpaid at period end	1,095	570
Equipment acquired under capital lease	1,149	—

See accompanying notes to condensed consolidated financial statements

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1. Description of Business and Summary of Significant Accounting Policies

Description of Business

RingCentral, Inc. (the "Company") is a provider of software-as-a-service ("SaaS") solutions for business communications. The Company was incorporated in California in 1999 and was reincorporated in Delaware on September 26, 2013. The Company is headquartered in San Mateo, California.

Public Offerings

On October 2, 2013, the Company completed its initial public offering (the "IPO") and sold 8,625,000 shares of Class A common stock to the public, including the underwriters' overallotment option of 1,125,000 shares of Class A common stock and 80,000 shares of Class A common stock sold by selling stockholders, at a price of $13.00 per share. The offer and sale of all of the shares in the IPO were registered under the Securities Act pursuant to a registration statement on Form S-1 (File No. 333-190815) (the "Initial Registration Statement"). The Company received aggregate proceeds of $103,309,000 from the IPO, net of underwriters' discounts and commissions, but before deduction of offering expenses of approximately $3,888,000.

On March 11, 2014, the Company completed a secondary public offering and sold 7,991,551 shares of Class A common stock to the public, including 791,551 of the underwriters' overallotment option and 5,200,000 shares of Class A common stock sold by selling stockholders, at a price of $21.50 per share. The offer and sale of all of the shares in the secondary public offering were registered under the Securities Act pursuant to a registration statement on Form S-1 (File No. 333-194132) (the "Secondary Registration Statement"). The Company received aggregate proceeds of $57,167,000 from the secondary public offering, net of underwriters' discounts and commissions, but before deduction of offering expenses of approximately $1,050,000.

Basis of Presentation

The unaudited condensed consolidated financial statements and accompanying notes of the Company reflect all adjustments (all of which are normal and recurring in nature) that, in the opinion of management, are necessary for a fair presentation of the interim periods presented. All intercompany balances and transactions have been eliminated in consolidation. The results of operations for the interim periods presented are not necessarily indicative of the results to be expected for any subsequent quarter or for the entire year ending December 31, 2014. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP") have been condensed or omitted under the rules and regulations of the Securities and Exchange Commission (the "SEC").

The unaudited interim condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and related notes for the fiscal year ended December 31, 2013 included in the Company's fiscal 2013 Annual Report on Form 10-K. There have been no changes in the Company's significant accounting policies from those that were disclosed in the Company's audited consolidated financial statements for the fiscal year ended December 31, 2013.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The significant estimates made by management affect revenues, accounts receivable, the allowance for doubtful accounts, inventory and inventory reserves, share-based compensation, deferred revenue, return reserves, provision for income taxes, uncertain tax positions, loss contingencies, sales tax liabilities and accrued liabilities. Management periodically evaluates such estimates and they are adjusted prospectively based upon such periodic evaluation. Actual results could differ from those estimates.

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers (Topic 606). The new guidance is a result of a joint project with the International Accounting Standards Board (the "IASB") to clarify and converge the revenue recognition principles under U.S. GAAP and IFRS and to develop guidance that would streamline and enhance revenue recognition requirements. Entities have the option of using either a full retrospective or modified retrospective approach for the adoption of the standard. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. The Company is currently evaluating the impact that the standard will have on its consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

In June 2014, the FASB issued ASU No. 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. The new standard requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. As such, the performance target should not be reflected in estimating the grand-date fair value of the award. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2014. The Company believes the adoption of this standard will not have a material impact on its consolidated financial statements because it does not anticipate granting share-based payment awards with performance targets that can be achieved after the requisite service period.

Note 2. Financial Statement Components

Cash and cash equivalents consisted of the following (in thousands):

	September 30, 2014	December 31, 2013
Cash	$ 20,338	$ 34,561
Money market funds	100,353	81,817
Total cash and cash equivalents	$ 120,691	$ 116,378

Accounts receivable, net consisted of the following (in thousands):

	September 30, 2014	December 31, 2013
Accounts receivable	$ 6,058	$ 2,192
Unbilled accounts receivable	1,490	992
Allowance for doubtful accounts	(105)	(139)
Accounts receivable, net	$ 7,443	$ 3,045

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

	September 30, 2014	December 31, 2013
Computer hardware and software	$ 43,271	$ 30,449
Internal-use software development costs	5,283	4,636
Furniture and fixtures	1,997	1,127
Leasehold improvements	2,866	859
Property and equipment, gross	53,417	37,071
Less: accumulated depreciation	(27,555)	(20,411)
Property and equipment, net	$ 25,862	$ 16,660

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Accrued liabilities consisted of (in thousands):

	September 30, 2014	December 31, 2013
Accrued compensation and benefits	$ 8,874	$ 5,660
Accrued sales, use and telecom related taxes	5,963	3,967
Accrued expenses	15,554	10,168
Other	1,268	764
Total accrued liabilities	$ 31,659	$ 20,559

Note 3. Fair Value of Financial Instruments

The Company carries certain financial assets consisting of money market funds, certificates of deposit, commercial paper and corporate debt securities at fair value on a recurring basis. Fair value is based on the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is estimated by applying the following hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

Level 1: Observable inputs which include unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2: Observable inputs other than Level 1 inputs, such as quoted prices for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3: Unobservable inputs that are supported by little or no market activity and that are based on management’s assumptions, including fair value measurements determined by using pricing models, discounted cash flow methodologies or similar techniques.

The fair value of assets carried at fair value was determined using the following inputs (in thousands):

	Balance at September 30, 2014	(Level 1)	(Level 2)	(Level 3)
Cash equivalents:				
Money market funds	$ 100,353	$ 94,057	$ 6,296	$ —
Short-term investments:				
Corporate debt securities	$ 26,666	$ 26,666	$—	$ —
Commercial paper	$ 1,996	$—	$ 1,996	$ —

Other assets:				
Certificates of deposit	$ 630	$—	$630	$ —

	Balance at December 31, 2013	(Level 1)	(Level 2)	(Level 3)
Cash equivalents:				
Money market funds	$ 81,817	$72,717	$9,000	$ —
Other assets:				
Certificates of deposit	$ 630	$—	$630	$ —

During the three months ended September 30, 2014, the Company purchased investments in commercial paper and corporate debt securities with original maturities ranging from 4 to 15 months. Management determines the appropriate categorization of its investments at the time of purchase and reevaluates classification at each reporting date. At September 30, 2014, all investments were designated as available-for-sale and reported at fair value based either upon quoted prices in active markets, quoted prices in less active markets, or quoted market prices for similar investments, with unrealized gains and losses, net of related tax, if any, included in other comprehensive loss. We may sell these securities at any time for use in current operations or for other purposes, such as consideration for acquisitions, even if they have not yet reached maturity. As a result, all of our investments held at September 30, 2014, including securities with maturities beyond twelve months, were classified as current assets in the accompanying condensed consolidated balance sheet.

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

At September 30, 2014, available-for-sale securities consisted of the following (in thousands):

	Available-for-Sale Securities			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate debt securities	$26,700	$ —	$ (34)	$ 26,666
Commercial paper	1,996	—	—	1,996
Total	$28,696	$ —	$ (34)	$ 28,662

The expected maturities of our investments in available-for-sale securities at September 30, 2014 are shown below (in thousands):

Available-for-Sale Securities	Amortized Cost	Estimated Fair Value
Due in less than one year	$ 26,362	$ 26,331
Due in one to five years	2,334	2,331
Total	$ 28,696	$ 28,662

The Company’s other financial instruments, including accounts receivable, accounts payable and other current liabilities, are carried at cost which approximates fair value due to the relatively short maturity of those instruments. Based on borrowing rates available to the Company for loans with similar terms, the stable interest rate environment and considering our credit risks, the carrying value of debt approximates fair value.

Note 4. Debt

As of September 30, 2014, the Company’s debt is comprised of borrowings under loan and security agreements, as amended, with Silicon Valley Bank (“SVB”) and TriplePoint Capital LLC (“TriplePoint”).

SVB Loan Agreement

Under the SVB agreement, the Company has two outstanding growth capital term loans (i.e., “the 2012 term loan” and “the 2013 term loan”), and a revolving line of credit.

The 2012 term loan was borrowed in March 2012 with a principal amount of $8,000,000, which is being repaid in 36 equal monthly installments of principal and interest. Under the 2012 term loan, interest is paid monthly and accrues at a floating rate based on the Company’s option of the (i) prime rate plus a margin of 0.25% or 0.50% or (ii) adjusted LIBOR rate (based on one, two, three or six-month interest periods) plus a margin of 3.25% or 3.50%, in each case such margin being determined based on cash balances maintained with SVB. The Company elected the prime rate option and, based on cash balances maintained with SVB at September 30, 2014, the current interest rate is 3.5%. In addition, a final terminal payment equal to 0.5% of the original loan principal, or $40,000, is due at maturity. The remaining principal balance and the final terminal payment are classified as current liabilities in the accompanying condensed consolidated balance sheet because the loan matures March 2015. As of September 30, 2014, the outstanding principal balance of the 2012 term loan was $1,333,000. As of September 30, 2014, the unamortized discount on the 2012 term loan was $6,000 which is recorded in the current portion of long-term debt line in the accompanying condensed consolidated balance sheet.

The 2013 term loan was borrowed on December 31, 2013 with a principal amount of $15,000,000, which is being repaid in 48 equal monthly installments of principal and interest. Interest is due monthly and accrues at a floating rate based on the Company’s option of an annual rate of either the (i) prime rate plus a margin of 0.75% or 1.00% or (ii) adjusted LIBOR rate (based on one, two, three or six-month interest periods) plus a margin of 3.75% or 4.00%, in each case such margin being determined based on cash balances maintained with SVB. The Company elected the prime rate option and based on cash balances maintained with SVB at September 30, 2014, the current interest rate is 4.0%. As of September 30, 2014, the outstanding principal balance of the 2013 term loan was $12,500,000.

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

The revolving line of credit provides for a maximum borrowing of up to $15,000,000 subject to limits based on the outstanding principal balance of the 2012 term loan and recurring subscription revenue amounts as defined in the agreement. The recurring subscription revenue requirement is not expected to limit the amount of borrowings available under the line of credit. Under the line of credit, interest is paid monthly and accrues at a floating rate based on the Company’s option of the (i) prime rate plus a margin of 0.25% or 0.50% or (ii) adjusted LIBOR rate (based on one, two, three or six-month interest periods) plus a margin of 3.25% or 3.50%, in each case such margin being determined based on cash balances maintained with SVB. The Company elected the prime rate option and based on cash balances maintained with SVB at September 30, 2014, the current interest rate is 3.5%. All outstanding principal and unpaid interest must be repaid by August 13, 2015. The outstanding principal balance is classified as a current liability in the accompanying condensed consolidated balance sheet because the loan matures August 2015. As of September 30, 2014, the outstanding principal balance and the available borrowing capacity of the line of credit were $10,778,000 and $2,889,000, respectively. As of September 30, 2014, the unamortized discount on the revolving line of credit was $205,000 which is recorded in the current portion of long-term debt line in the accompanying condensed consolidated balance sheet.

The Company has pledged all of its assets, excluding intellectual property, as collateral to secure its obligations under the SVB agreement. The SVB agreement contains customary negative covenants that limit the Company’s ability to, among other things, incur additional indebtedness, grant liens, make investments, repurchase stock, pay dividends, transfer assets and merge or consolidate. The SVB agreement also contains customary affirmative covenants, including requirements to, among other things, (i) maintain minimum cash balances representing the greater of $10,000,000 or three times the Company’s quarterly cash burn rate, as defined in the agreement, and (ii) maintain minimum EBITDA levels, as determined in accordance with the agreement. On June 17, 2014, the Company adjusted certain financial covenant thresholds to expand its ability to invest in certain foreign subsidiaries. The Company was in compliance with all covenants under its credit agreement with SVB as of September 30, 2014.

TriplePoint Loan Agreement

Under the equipment loan and security agreement with TriplePoint, the Company borrowed equipment term loans with aggregate principal of $9,691,000 in August 2012. The equipment term loans are being repaid in 36 equal monthly installments of principal and interest, which accrues at an annual fixed rate of 5.75%. In addition, a final terminal payment is due at maturity equal to 10% of the original loan principal, or $970,000. The remaining principal balance and the final terminal payment are classified as current liabilities in the accompanying condensed consolidated balance sheet because the loan matures August 2015. As of September 30, 2014, the outstanding principal balance of the TriplePoint equipment term loan was $2,848,000. As of September 30, 2014, the unamortized discount on the revolving line of credit was $9,000 which is recorded in the current portion of long-term debt line in the accompanying condensed consolidated balance sheet.

The TriplePoint equipment loan and security agreement contains customary negative covenants that limit the Company’s ability to, among other things, incur additional indebtedness, grant liens, make investments, repurchase stock, pay dividends, transfer assets and merge or consolidate. The TriplePoint equipment loan and security agreement also contain customary affirmative covenants, including requirements to, among other things, deliver audited financial statements. On June 17, 2014, the Company adjusted certain financial covenant thresholds to expand its ability to invest in certain foreign subsidiaries. The Company was in compliance with all covenants under its credit agreements with TriplePoint as of September 30, 2014.

12

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 5. Commitments and Contingencies

Leases

The Company leases facilities for office space under noncancelable operating leases for its U.S. and international locations and has entered into capital lease arrangements to obtain property and equipment for its operations. In addition, the Company leases space from third party datacenter hosting facilities under co-location agreements to support its cloud infrastructure. In March 2014, the Company entered into a new lease for its office in Denver, Colorado for a total lease commitment of $4,653,000 through 2019 and lease incentives totaling $1,159,000. In May 2014, the Company entered into a new lease for its office in London, England for a total lease commitment of approximately $1,941,000 through 2019 with an option to extend through 2024. On September 25 2014, the Company entered into a new lease for its headquarters for a total lease commitment of $17,497,000 through 2021 and lease incentives totaling $1,486,000. The Company is currently occupying a small portion of the building and will take possession of the remainder of the building sometime in the first quarter of fiscal 2015. All agreements contain escalating monthly rental payments over the lease term, which will be amortized to rent expense on a straight-line basis over the lease term.

Sales Tax Liability

During 2010 and 2011, the Company increased its sales and marketing activities in the U.S., which may be asserted by a number of states to create an obligation under nexus regulations to collect sales taxes on sales to customers in the state. Prior to 2012, the Company did not collect sales taxes from customers on sales in all states. In the second quarter of 2012, the Company commenced collecting and remitting sales taxes on sales in all states so a loss contingency related to sales taxes exists for sales and marketing activities in 2010, 2011 and the six months ended June 30, 2012. As of September 30, 2014 and December 31, 2013, the Company had a balance for a long-term sales tax liability of $3,953,000 and $3,988,000, respectively, based on its best estimate of the probable liability for the loss contingency incurred as of those dates. The Company’s estimate of a probable outcome under the loss contingency is based on analysis of its sales and marketing activities, revenues subject to sales tax, and applicable regulations in each state in each period. No significant adjustments to the long-term sales tax liability have been recognized in the accompanying condensed consolidated financial statements for changes to the assumptions underlying the estimate. However, changes in management’s assumptions may occur in the future as the Company obtains new information which can result in adjustments to the recorded liability. Increases and decreases to the long-term sales tax liability are recorded as general and administrative expense.

A current sales tax liability for noncontingent amounts expected to be remitted in the next twelve months of $4,441,000 and $3,451,000, is included in accrued liabilities as of September 30, 2014 and December 31, 2013, respectively.

Legal Matters

The Company determines whether an estimated loss from a contingency should be accrued by assessing whether a loss is deemed probable and can be reasonably estimated. The Company assesses its potential liability by analyzing specific litigation and regulatory matters using reasonably available information. The Company develops its views on estimated losses in consultation with inside and outside counsel, which involves a subjective analysis of potential results and outcomes, assuming various combinations of appropriate litigation and settlement strategies. Legal fees are expensed in the period in which they are incurred. As of September 30, 2014 and December 31, 2013, there were no significant ongoing legal matters and the Company did not have any accrued liabilities recorded for such loss contingencies.

Note 6. Share-Based Compensation

A summary of share-based compensation expense recognized in the Company's consolidated statements of operations follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Cost of services revenues	$330	$129	$974	$297
Research and development	926	367	2,426	884
Sales and marketing	1,396	330	3,661	734
General and administrative	1,546	1,384	4,245	2,631
Total share-based compensation expense	$4,198	$2,210	$11,306	$4,546

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

A summary of share-based compensation expense by award type follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Options	$2,740	$2,210	$7,812	$4,546
Employee stock purchase plan rights	273	—	1,203	—
Restricted stock units	1,185	—	2,291	—
Total share-based compensation expense	$4,198	$2,210	$11,306	$4,546

As of September 30, 2014 and December 31, 2013, there was approximately $20,456,000 and $22,439,000 of unrecognized share-based compensation expense, net of estimated forfeitures, related to nonvested stock option grants, which will be recognized on a straight-line basis over the remaining weighted-average vesting periods of approximately 2.5 years and 3.0 years, respectively.

Equity Incentive Plans

As of September 30, 2014 a total of 7,567,000 shares remained available for grant under the 2013 Plan. A summary of option activity under all of the Company's equity incentive plans at September 30, 2014 and changes during the period then ended is presented in the following table:

	Number of Options Outstanding (in thousands)	Weighted-Average Exercise Price Per Share	Weighted-Average Contractual Term (in Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2013	11,156	$ 5.87	7.7	$ 139,484
Granted	935	15.88		
Exercised	(2,437)	1.87		
Canceled/Forfeited	(476)	6.03		
Outstanding at September 30, 2014	9,178	$ 7.95	7.4	$ 47,452
Vested and expected to vest as of September 30, 2014	8,765	$ 7.84	7.4	$ 46,456
Exercisable as of September 30, 2014	4,730	$ 5.20	6.8	$ 36,024

The weighted average grant date fair value of options granted and the total intrinsic value of options exercised were as follows (in thousands, except weighted average grant date fair value):

	Three Months Ended September 30, 2014	2013	Nine Months Ended September 30, 2014	2013
Weighted average grant date fair value per share	$5.56	$6.75	$6.42	$6.08
Total intrinsic value of options exercised	$3,944	$6,028	$26,429	$9,855

The Company estimated the fair values of each option awarded on the date of grant using the Black-Scholes option pricing model, which requires inputs including the fair value of common stock, expected term, expected volatility, risk-free interest and dividend yield. The weighted-average assumptions used in the option pricing models in the periods presented were as follows:

	Three Months Ended September 30, 2014	2013	Nine Months Ended September 30, 2014	2013
Expected term for employees (in years)	4.6	6.1	4.4	6.1
Expected term for non-employees (in years)	7.0	10.0	7.0	10.0
Risk-free interest rate	1.56%	1.99%	1.38%	1.68%
Expected volatility	47 %	54 %	48 %	54 %
Expected dividend rate	0 %	0 %	0 %	0 %

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

On January 29, 2014, the Compensation Committee of the Board of Directors approved an amendment to the 2013 Plan to decrease the contractual term of all equity awards issued from the 2013 Plan from 10 years to 7 years for all awards granted after January 29, 2014.

Employee Stock Purchase Plan

The ESPP allows eligible employees to purchase shares of the Class A common stock at a discount through payroll deductions of up to the lesser of 15% of their eligible compensation or $25,000 per calendar year, at not less than 90% of the fair market value, as defined in the ESPP, subject to any plan limitations. A participant may purchase a maximum of 3,000 shares during an offering period. The offering period starts on the first trading day on or after May 11th and November 11th of each year, except that the first offering period commenced on the first trading day following the effective date of the Company’s Initial Registration Statement, and the offering period ends six months after the beginning of the offering period, on the last trading day on or after May 10th and November 10th of each year. At the end of the offering period, the purchase price is set at the lower of: (i) 90% of the fair value of the Company’s common stock at the beginning of the six month offering period, and (ii) 90% of the fair value of the Company’s common stock at the end of the six month offering period. As of September 30, 2014, there was a total of $122,000 of unrecognized share-based compensation expense, net of estimated forfeitures, related to ESPP, which will be recognized on a straight-line basis over the remaining weighted-average vesting period of approximately 0.1 years. At September 30, 2014, a total of 1,658,000 shares were available for issuance under the ESPP.

Restricted Stock Units

For the three and nine months ended September 30, 2014, we issued 266,000 and 1,192,000 restricted stock units of Class A common stock under the 2013 Plan with a weighted average grant date fair value of $13.61 and $16.35 per share. No restricted stock units were issued during the nine months ended September 30, 2013. As of September 30, 2014, there was a total of $18,030,000 of unrecognized share-based compensation expense, net of estimated forfeitures, related to restricted stock units, which will be recognized on a straight-line basis over the remaining weighted-average vesting period of approximately 3.6 years.

Note 7. Concentrations

Revenue by geographic location is based on the billing address of the customer. More than 90% of the Company’s revenue is from the United States during the three and nine months ended September 30, 2014 and 2013. Property and equipment by geographic location is based on the location of the legal entity that owns the asset. At September 30, 2014 and December 31, 2013, more than 87% and 84%, respectively, of the Company’s property and equipment was located in the United States, with no single country outside the United States representing more than 10% of property and equipment.

Note 8. Income Taxes

The provision (benefit) for income taxes for the three and nine months ended September 30, 2014 and 2013, was $19,000, $54,000, $184,000, and ($66,000), respectively. The provision for income taxes during the three and nine months ended September 30, 2014 and the three months ended September 30, 2013 consisted primarily of state minimum taxes, and foreign income taxes. The benefit for income taxes during the nine months ended September 30, 2013 consisted of foreign income taxes, state minimum taxes and recognition of a foreign tax credit.

For the three and nine months ended September 30, 2014 and 2013, the provision for income taxes differed from the U.S federal statutory amount primarily due to state and foreign taxes currently payable, and the Company realized no benefit for current year losses due to maintaining a full valuation allowance against the U.S. and foreign net deferred tax assets.

The realization of tax benefits of deferred tax assets is dependent upon future levels of taxable income, of an appropriate character, in the periods the items are expected to be deductible or taxable. Based on the available objective evidence, the Company does not believe it is more likely than not that the net deferred tax assets will be realizable. Accordingly, the Company has provided a full valuation allowance against all of the domestic and the majority of the foreign net deferred tax assets as of September 30, 2014 and December 31, 2013. The Company intends to maintain the full valuation allowance until sufficient positive evidence exists to support a reversal of, or decrease in, the valuation allowance.

During the three and nine months ended September 30, 2014, there have been no material changes to the total amount of unrecognized tax benefits.

RINGCENTRAL, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 9. Basic and Diluted Net Loss Per Share

Basic net loss per share is computed by dividing the net loss by the weighted-average number of shares of common stock outstanding during the period, less the weighted-average unvested common stock subject to repurchase or forfeiture as they are not deemed to be issued for accounting purposes. Diluted net loss per share is computed by giving effect to all potential shares of common stock, including preferred stock, warrants to purchase common and preferred stock, stock options and restricted stock units, to the extent they are dilutive. Upon the effectiveness of the Initial Registration Statement and the filing of its Certificate of Incorporation in Delaware on September 26, 2013, all outstanding preferred stock and warrants to purchase preferred stock were converted to common stock and warrants to purchase common stock, respectively. For the three and nine months ended September 30, 2014 and 2013, all such common stock equivalents have been excluded from diluted net loss per share as the effect to net loss per share would be anti-dilutive.

The following table sets forth the computation of the Company's basic and diluted net loss per share of common stock (in thousands, except per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Numerator				
Net loss	$(11,986)	$(8,852)	$(38,220)	$(32,732)
Denominator				
Weighted-average common shares for basic and diluted net loss per share	67,800	24,452	66,313	23,290
Basic and diluted net loss per share	$(0.18)	$(0.36)	$(0.58)	$(1.41)

The following table sets forth the potential shares of common stock that were excluded from diluted weighted-average common shares outstanding (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Shares of common stock issuable upon conversion of warrants	—	502	—	502
Shares of common stock subject to repurchase	18	49	18	49

Shares of common stock issuable under equity incentive awards outstanding	10,284	11,085	10,284	11,085
Potential common shares excluded from diluted net loss per share	10,302	11,636	10,302	11,636

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K filed on February 26, 2014 under the Securities Act of 1934, as amended (the "Securities Act") with the SEC. As discussed in the section titled "Special Note Regarding Forward-Looking Statements," the following discussion and analysis contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" included under Part II, Item 1A below.

Overview

We are a leading provider of software-as-a-service, or SaaS, solutions for business communications. We believe that our innovative, cloud-based approach disrupts the large market for business communications solutions by providing flexible and cost-effective services that support distributed workforces, mobile employees and the proliferation of "bring-your-own" communications devices. We enable convenient and effective communications for our customers, across all their locations, all their employees, all the time, thus enabling a more productive and dynamic workforce. RingCentral Office, our flagship service, is a multi-user, enterprise-grade communications solution that enables our customers and their employees to communicate via different channels and on multiple devices, including smartphones, tablets, PCs and desk phones. We sell RingCentral Office in three editions: Standard, Premium and Enterprise. Our Standard Edition of RingCentral Office includes call management, mobile applications, voice, business SMS, integration with Dropbox, Box, Google Drive and Microsoft Office and Outlook, and conferencing capabilities. Our Premium Edition includes the Standard Edition functionality together with Salesforce CRM integration, automatic call recording and premium support. Our Enterprise Edition was launched in 2013 which includes the Premium Edition functionality together with multipoint HD video and web conferencing and online meetings functionality. During May 2014, these new features (multipoint HD video and web conferencing and online meetings) were added to our Standard and Premium editions. All editions vary in the number of toll-free minutes and number of meeting attendees.

We primarily generate revenues by selling subscriptions for our RingCentral Office, RingCentral Professional, and RingCentral Fax offerings. RingCentral Office is offered at monthly subscription rates, varying with the specific functionalities and services and the number of users. RingCentral Office customers generally pay higher monthly subscription rates than customers of our other service offerings. RingCentral Professional is offered at monthly subscription rates that vary based on the desired number of minutes usage and extensions allotted to the plan. RingCentral Fax is offered at monthly subscription rates that vary based on the desired number of pages and phone numbers allotted to the plan.

Our subscription plans have historically had monthly or annual contractual terms and approximately 90% of our current customers are on monthly contractual terms, although we also have subscription plans with multi-year contractual terms, generally with larger customers. We believe that this flexibility in contract duration is important to meet the different needs of our customers. Generally, our fees for subscription plans have been billed in advance via credit card. However, as the number of RingCentral Office customers with more users grows, we expect to bill more customers through commercial invoices with customary payment terms and, accordingly, our levels of accounts receivable may increase. A significant component of our accounts receivable is derived from resellers. For the three and nine months ended September 30, 2014 and 2013, services revenues accounted for more than 90% of our total revenues. The remainder of our revenues is primarily comprised of product revenues from the sale of pre-configured office phones, which we offer as a convenience to our customers in connection with subscriptions to our services.

Beginning in 2009, in connection with our introduction of RingCentral Office, we established a direct, inside sales force. Since then, we have continued investing in our direct, inside sales force while also developing indirect sales channels to market our brand and our service offerings. Our indirect sales channel consists of a network of over 1,500 sales agents and resellers, including AT&T, which we refer to collectively as resellers. We intend to continue to foster this network and to expand our network with other resellers. In 2014, we entered into agreements with TELUS Communications Company, or TELUS, and British Telecommunications plc, or BT, to expand our indirect sales channel in Canada and the United Kingdom, respectively.

Since its launch, our revenue growth has primarily been driven by our flagship RingCentral Office service offering, which has resulted in an increased number of customers, increased average subscription revenues per customer, and increased retention of our existing customer and user base. We define a “customer” as one individual billing relationship for the subscription to our services, which generally correlates to one company account per customer. We define a user as one person within a customer who has been granted a subscription license to use our services, such that the number of users per customer generally correlates closely to the number of employees within a customer account. As of September 30, 2014, we had over 300,000 customers from industries including advertising, finance, healthcare, legal services, non-profit organizations, real estate, retail and technology, and ranging in size from businesses with fewer than 10 users to more than 1,500 users. In October of 2013, we launched RingCentral Office in the United Kingdom. For the three and nine months ended September 30, 2014 and 2013, 99% of our total revenues were generated in the U.S. and Canada, although we expect the percentage of our total revenues derived outside of the U.S. and Canada to grow as we expand internationally in the United Kingdom and beyond.

The growth of our business and our future success depend on many factors, including our ability to expand our customer base to medium-sized and larger customers, continue to innovate, grow revenues from our existing customer base, expand our distribution channels and scale internationally. For example, as a result of our efforts to expand our customer base to target medium-sized and larger businesses, we expect to incur additional research and development and support and professional services costs and may experience longer sales cycles that may delay revenues associated with these costs. Furthermore, because we have limited experience selling to larger businesses and international customers, our investment in marketing our services to these potential customers may not be successful, which could materially and adversely affect our results of operations and our overall ability to grow our customer base. While these areas represent significant opportunities for us, they also pose risks and challenges that we must successfully address in order to sustain the growth of our business and improve our operating results. In addition, there has been and may be in the future substantial litigation in the areas in which we operate regarding intellectual property rights, including third parties claiming patent infringement, to which we have been subjected in the past and may be subjected in the future. We cannot assure you that we will be successful in defending against any such claims or that we will be able to settle any such claims or that any such settlement would be on terms that are favorable to us.

We have experienced significant growth in recent periods, with total revenues of $78.9 million, $114.5 million and $160.5 million in 2011, 2012 and 2013, respectively, generating year-over-year increases of 45% and 40%, respectively. We have continued to make significant expenditures and investments, including those in research and development, infrastructure and operations and incurred net losses of $13.9 million, $35.4 million and $46.1 million, in 2011, 2012 and 2013, respectively. For the three months ended September 30, 2014 and 2013, our total revenues were $56.9 million and $41.9 million, respectively, representing a year-over-year increase of 36%. For the nine months ended September 30, 2014 and 2013, our total revenues were $158.0 million and $115.2 million, respectively, representing a year-over-year increase of 37%. For the three months ended September 30, 2014 and 2013, our net losses were $12.0 million and $8.9 million, respectively, and for the nine months ended September 30, 2014 and 2013, our net losses were $38.2 million and $32.7 million, respectively.

Key Business Metrics

In addition to generally accepted accounting principles, or U.S. GAAP, financial measures such as total revenues, gross margin and cash flows from operations, we regularly review a number of key business metrics to evaluate growth trends, measure our performance, and make strategic decisions. We discuss revenues and gross margin under “Results of Operations” and cash flow from operations under “Liquidity and Capital Resources.” Other key business metrics are discussed below.

Annualized Exit Monthly Recurring Subscriptions

We believe that our Annualized Exit Monthly Recurring Subscriptions is a leading indicator of our anticipated services revenues. We believe that trends in revenue are important to understanding the overall health of our marketplace, and we use these trends in order to formulate financial projections and make strategic business decisions. Our Annualized Exit Monthly Recurring Subscriptions equals our Monthly Recurring Subscriptions multiplied by 12. Our Monthly Recurring Subscriptions equals the monthly value of all customer subscriptions in effect at the end of a given month. For example, our Monthly Recurring Subscriptions at September 30, 2014 were $18.3 million. As such, our Annualized Exit Monthly Recurring Subscriptions at September 30, 2014 were $219.8 million.

RingCentral Office Annualized Exit Monthly Recurring Subscriptions

We calculate our RingCentral Office Annualized Exit Monthly Recurring Subscriptions in the same manner as we calculate our Annualized Exit Monthly Recurring Subscriptions, except that only customer subscriptions from RingCentral Office customers are included when determining Monthly Recurring Subscriptions for the purposes of calculating this key business metric. RingCentral Office is our flagship service offering. We believe that trends in revenue with respect to RingCentral Office are also important to understanding the overall health of our marketplace, and we use these trends in order to formulate financial projections and make strategic business decisions. Our RingCentral Office Annualized Exit Monthly Recurring Subscriptions at September 30, 2014 were $153.7 million.

Net Monthly Subscription Dollar Retention Rate

We believe that our Net Monthly Subscription Dollar Retention Rate provides insight into our ability to retain and grow services revenues, as well as our customers' potential long-term value to us. We believe that our ability to retain our customers and expand their use of our solutions over time is a leading indicator of the stability of our revenue base and we use these trends in order to formulate financial projections and make strategic business decisions. We define our Net Monthly Subscription Dollar Retention Rate as (i) one plus (ii) the quotient of Dollar Net Change divided by Average Dollar Monthly Recurring Subscriptions.

We define Dollar Net Change as the quotient of (i) the difference of our Monthly Recurring Subscriptions at the end of a period minus our Monthly Recurring Subscriptions at the beginning of a period minus our Monthly Recurring Subscriptions at the end of the period from new customers we added during the period, (ii) all divided by the number of months in the period. We define our Average Monthly Recurring Subscriptions as the average of the Monthly Recurring Subscriptions at the beginning and end of the measurement period.

As an illustrative example, if our Monthly Recurring Subscriptions were $118 at the end of a quarterly period and $100 at the beginning of period, and $20 at the end of the period from new customers we added during the period, then the Dollar Net Change would be equal to ($0.67), or the amount equal to the difference of $118 minus $100 minus $20, all divided by three months. Our Average Monthly Recurring Subscriptions would equal $109, or the sum of $100 plus $118, divided by two. Our Net Monthly Subscription Dollar Retention Rate would then equal 99.4%, or approximately 99%, or one plus the quotient of the Dollar Net Change divided by the Average Monthly Recurring Subscriptions.

Our key business metrics for the five quarterly periods ended September 30, 2014 were as follows (dollars in millions):

	September 30, 2014	June 30, 2014	March 31, 2014	December 31, 2013	September 30, 2013
Net Monthly Subscription Dollar Retention Rate	>99%	>99%	~99%	~99%	~99%
Annualized Exit Monthly Recurring Subscriptions	$ 219.8	$ 203.7	$ 187.7	$ 173.2	$ 160.6
RingCentral Office Annualized Exit Monthly Recurring Subscriptions	$ 153.7	$ 139.2	$ 125.8	$ 112.3	$ 100.5

Results of Operations

The following tables show our results of operations in dollars and as a percentage of our total revenues. The historical results presented below are not necessarily indicative of the results that may be expected for any future period (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenues:				
Services	$51,951	$37,925	$143,668	