AKAMAI TECHNOLOGIES INC
Form 10-Q
August 11, 2008
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 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 June 30, 2008

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 0-27275

Akamai Technologies, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**04-3432319**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

8 Cambridge Center

Cambridge, MA 02142

(617) 444-3000

(Address, Including Zip Code, and Telephone Number,

Including Area Code, of Registrant s Principal Executive Offices)

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

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

Large accelerated filer x	Accelerated Filer ¨	Non-accelerated Filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

The number of shares outstanding of the registrant s common stock as of August 7, 2008: 169,118,648 shares.

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AKAMAI TECHNOLOGIES, INC.

FORM 10-Q

For the quarterly period ended June 30, 2008

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PART I. FINANCIAL INFORMATION

Item 1. *Financial Statements*

AKAMAI TECHNOLOGIES, INC.

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

	June 30, 2008	December 31, 2007
	(In thousands, except share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 165,417	$ 145,078
Marketable securities (including restricted securities of $3,460 at June 30, 2008 and $511 at December 31, 2007)	126,280	401,091
Accounts receivable, net of reserves of $8,143 at June 30, 2008 and $10,391 at December 31, 2007	125,765	118,944
Prepaid expenses and other current assets	30,608	23,782
Deferred income tax assets	6,147	6,147
Total current assets	454,217	695,042
Property and equipment, net	158,067	134,546
Marketable securities (including restricted securities of $153 at June 30, 2008 and $3,102 at December 31, 2007)	453,945	87,339
Goodwill	361,645	361,637
Other intangible assets, net	80,419	87,500
Deferred income tax assets, net	241,621	285,463
Other assets	5,503	4,520
Total assets	$ 1,755,417	$ 1,656,047
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 25,852	$ 18,540
Accrued expenses and other current liabilities	41,434	56,233
Deferred revenue	13,993	12,995
Accrued restructuring	63	607
Total current liabilities	81,342	88,375
Other liabilities	9,878	7,812
Deferred revenue	1,745	1,453
1% convertible senior notes	199,855	199,855
Total liabilities	292,820	297,495
Commitments, contingencies and guarantees (Note 15)		
Stockholders equity:		

Preferred stock, $0.01 par value; 5,000,000 shares authorized; 700,000 shares designated as Series A Junior Participating Preferred Stock; none outstanding		
Common stock, $0.01 par value; 700,000,000 shares authorized; 168,912,020 and 166,212,638 shares issued and outstanding at June 30, 2008 and December 31, 2007, respectively	1,689	1,662
Additional paid-in capital	4,495,675	4,446,703
Accumulated other comprehensive (loss) income, net	(13,146)	3,053
Accumulated deficit	(3,021,621)	(3,092,866)
Total stockholders equity	1,462,597	1,358,552
Total liabilities and stockholders equity	$ 1,755,417	$ 1,656,047

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

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AKAMAI TECHNOLOGIES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
	(In thousands, except per share amounts)			
Revenues	$ 194,004	$ 152,654	$ 381,023	$ 291,928
Costs and operating expenses:				
Cost of revenues	53,688	39,759	105,263	74,239
Research and development	9,519	11,663	18,823	22,267
Sales and marketing	41,188	37,739	77,132	74,488
General and administrative	33,803	29,779	67,069	57,257
Amortization of other intangible assets	3,491	2,932	7,081	5,744
Restructuring benefit		(178)		(178)
Total costs and operating expenses	141,689	121,694	275,368	233,817
Income from operations	52,315	30,960	105,655	58,111
Interest income	5,490	6,015	13,531	11,518
Interest expense	(710)	(772)	(1,420)	(1,543)
Loss on early extinguishment of debt				(1)
Other (expense) income, net	(970)	(572)	(494)	(776)
Gain on investments, net	64		272	
Income before provision for income taxes	56,189	35,631	117,544	67,309
Provision for income taxes	21,855	13,985	46,299	26,484
Net income	$ 34,334	$ 21,646	$ 71,245	$ 40,825
Net income per weighted average share:				
Basic	$ 0.21	$ 0.13	$ 0.43	$ 0.25
Diluted	$ 0.19	$ 0.12	$ 0.38	$ 0.23
Shares used in per share calculations:				
Basic	167,417	164,798	166,688	163,184
Diluted	187,641	185,601	187,493	184,648

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

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AKAMAI TECHNOLOGIES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	For the Six Months Ended June 30, 2008	2007
	(In thousands)	
Cash flows from operating activities:		
Net income	$ 71,245	$ 40,825
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	46,058	32,427
Stock-based compensation expense	28,248	34,038
Provision for deferred income taxes, net	43,952	25,138
Amortization of deferred financing costs	420	420
Provision for doubtful accounts	736	1,109
Non-cash portion of loss on early extinguishment of debt		1
Non-cash portion of restructuring benefit		(178)
Excess tax benefits from stock-based compensation	(10,282)	(15,973)
(Gains) losses on investments and loss on disposal of property and equipment, net	(303)	40
Changes in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable	(5,708)	(11,497)
Prepaid expenses and other current assets	(8,815)	(5,433)
Accounts payable, accrued expenses and other current liabilities	(8,107)	(15,103)
Deferred revenue	1,099	3,114
Accrued restructuring	(543)	(1,496)
Other non-current assets and liabilities	(197)	1,216
Net cash provided by operating activities	157,803	88,648
Cash flows from investing activities:		
Purchases of property and equipment	(45,943)	(53,121)
Capitalization of internal-use software development costs	(12,579)	(8,114)
Purchases of short- and long-term marketable securities	(358,459)	(206,110)
Proceeds from sales of short- and long-term marketable securities	154,033	75,329
Proceeds from maturities of short- and long-term marketable securities	95,782	80,754
Cash of acquired businesses, net of cash paid		7,875
Proceeds from the sale of property and equipment	74	
Net cash used in investing activities	(167,092)	(103,387)
Cash flows from financing activities:		
Excess tax benefits from stock-based compensation	10,282	15,973
Payments on capital leases		(23)
Proceeds from the issuance of common stock under stock option and employee stock purchase plans	18,132	17,751
Net cash provided by financing activities	28,414	33,701
Effects of exchange rate changes on cash and cash equivalents	1,214	605
Net increase in cash and cash equivalents	20,339	19,567
Cash and cash equivalents at beginning of period	145,078	80,595

Cash and cash equivalents at end of period	$ 165,417	$ 100,162
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 999	$ 1,003
Cash paid for income taxes	7,211	1,314
Non-cash financing and investing activities:		
Capitalization of stock-based compensation as internal-use software, net of impairments	$ 3,591	$ 2,811
Common stock and vested stock options issued in connection with acquisition of businesses		171,957
Common stock issued upon conversion of 1% convertible senior notes		40
Common stock returned upon settlement of escrow claims related to prior business acquisitions	(952)	

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

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AKAMAI TECHNOLOGIES, INC.

NOTES TO UNAUDITED CONSOLIDATED

FINANCIAL STATEMENTS

1. Nature of Business and Basis of Presentation

Akamai Technologies, Inc. (Akamai or the Company) provides services for accelerating and improving the delivery of content and applications over the Internet. Akamai s globally distributed platform comprises thousands of servers in hundreds of networks in approximately 70 countries. The Company was incorporated in Delaware in 1998 and is headquartered in Cambridge, Massachusetts. Akamai currently operates in one industry segment: providing services for accelerating and improving delivery of content and applications over the Internet.

The accompanying interim consolidated financial statements are unaudited and have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. These financial statements include the accounts of Akamai and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in the accompanying financial statements.

Certain information and footnote disclosures normally included in the Company s annual audited consolidated financial statements and accompanying notes have been condensed or omitted in these interim financial statements. Accordingly, the consolidated financial statements included herein should be read in conjunction with the audited consolidated financial statements and accompanying notes included in Akamai s annual report on Form 10-K for the year ended December 31, 2007, filed with the Securities and Exchange Commission on February 29, 2008.

The results of operations presented in this quarterly report on Form 10-Q are not necessarily indicative of the results of operations that may be expected for future periods. In the opinion of management, these unaudited consolidated financial statements include all adjustments and accruals, consisting only of normal recurring adjustments that are necessary for a fair statement of the results of all interim periods reported herein.

2. Business Acquisition

Red Swoosh

On April 12, 2007, the Company acquired all of the outstanding common and preferred stock of Red Swoosh Inc. (Red Swoosh), including vested stock options, in exchange for approximately 350,000 shares of Akamai common stock. The purchase of Red Swoosh was intended to augment Akamai s distributed Internet presence by combining client-side file management and distribution software with the Company s existing network of edge servers. The aggregate purchase price was $18.7 million, which consisted of $18.4 million in shares of Akamai common stock, $4,000 in fair value of Akamai stock options issued, and transaction costs of $0.2 million, which primarily consisted of fees for legal services. In accordance with the Financial Accounting Standards Board s (FASB) Emerging Issues Task Force Issue No. 99-12, Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination (EITF No. 99-12), the value of the common stock issued in the transaction was calculated using the average closing price of the Company s common stock for the five-day period beginning two days before and ending two days after the date on which all material aspects of the transaction were agreed to by all parties and the acquisition was announced.

The acquisition of Red Swoosh was accounted for using the purchase method of accounting. The results of operations of the acquired business since April 12, 2007, the date of acquisition, are included in the consolidated financial statements of the Company since the acquisition date. The total purchase consideration was allocated to the assets acquired and liabilities assumed based on their estimated fair values as of the date of acquisition, as

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determined by management. The excess of the purchase price over the amounts allocated to assets acquired and liabilities assumed was recorded as goodwill. The value of the goodwill from this acquisition can be attributed to a number of business factors including, but not limited to, cost synergies expected to be realized and a trained technical workforce. In accordance with current accounting standards, goodwill associated with the Red Swoosh acquisition will not be amortized and will be tested for impairment at least annually as required by Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets (SFAS No. 142) (see Note 10).

The following table presents the allocation of the purchase price for Red Swoosh (in thousands):

Total consideration:	
Value of common stock issued	$ 18,449
Fair value of stock options issued	4
Transaction costs	237
Total purchase consideration	$ 18,690
Allocation of the purchase consideration:	
Current assets, including cash and cash equivalents of $2,677	$ 3,236
Long-term assets	14
Deferred tax assets	1,355
Identifiable intangible assets	3,731
Goodwill	13,188
Deferred tax liabilities	(1,458)
Other liabilities assumed	(1,376)
	$ 18,690

In determining the purchase price allocation, the Company considered, among other factors, its intention to use the acquired assets and the estimated future demand for the acquired technology. The fair value of identifiable intangible assets was based upon both the cost avoidance and opportunity cost savings approaches. The rate used to discount the expected future net cash flows from the intangible assets to their present values was based upon a weighted average cost of capital of 20%, with a tax rate of 40%. The discount rate was determined after consideration of market rates of return on debt and equity capital, the weighted average return on invested capital and the risk associated with achieving forecasted sales and cost savings related to the technology and assets acquired.

The Company valued the acquired completed technologies at $3.7 million, with a weighted average useful life of 4.4 years. The intangible assets are being amortized based upon the pattern in which the economic benefits of the intangible assets are being utilized, which in general reflects the cash flow savings from such assets. None of the goodwill or identifiable intangible assets resulting from the Red Swoosh acquisition are deductible for income tax purposes.

The consolidated financial statements include operating results from the date of acquisition. Pro forma results of operations for this acquisition have not been presented because the effects of the acquisition were not material to the Company s financial results.

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3. Recent Accounting Pronouncements

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115 (SFAS No. 159). SFAS No. 159 allows companies to measure certain financial assets and liabilities at fair value. The fair value option may be elected on an instrument-by-instrument basis and is irrevocable, unless a new election date occurs. If the fair value option is elected for an instrument, SFAS No. 159 specifies that unrealized gains and losses for that instrument shall be reported in earnings at each subsequent reporting date. SFAS No. 159 became effective on January 1, 2008. The Company adopted SFAS No. 159 on January 1, 2008 and elected not to measure eligible financial assets and liabilities at fair value. Accordingly, the adoption of SFAS No. 159 did not have a material impact on the Company s financial position and results of operations.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), Business Combinations (SFAS No. 141R). This statement establishes principles and requirements for how the acquirer in a business combination (i) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquired company, (ii) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase and (iii) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS No. 141R is effective for fiscal years beginning after December 15, 2008. The Company is currently evaluating the potential impact of SFAS No. 141R on its financial position and results of operations.

In April 2008, the FASB issued FASB Staff Position No. FAS 142-3 Determination of the Useful Life of Intangible Assets (FSP 142-3). FSP 142-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years; accordingly, the Company will adopt FSP 142-3 in fiscal year 2009. FSP 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142 Goodwill and Other Intangible Assets (FAS 142). FSP 142-3 is intended to improve the consistency between the useful life of an intangible asset determined under FAS 142 and the period of expected cash flows used to measure the fair value of the asset under FASB Statement No. 141R (revised 2007) Business Combinations and other United States generally accepted accounting principles. The Company is currently evaluating the impact, if any, of the adoption of FSP 142-3 on its consolidated financial position, results of operations and cash flows.

4. Investments and Fair Value

Effective January 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements (SFAS No. 157), which establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 clarifies that fair value is an exchange price, representing the amount that would be received in an orderly transaction between market participants, upon the sale of an asset or a payment to transfer a liability (an exit price) in the principal or most advantageous market for such asset or liability in an orderly transaction between market participants. In February 2008, the FASB issued Staff Position FAS No. 157-2, Partial Deferral of the Effective Date of Statement No. 157 (FSP No. 157-2). FSP No. 157-2 delays the effective date of SFAS No. 157 for non-financial assets and liabilities that are not measured or disclosed on a recurring basis until fiscal years beginning after November 15, 2008. To date, therefore, the Company has adopted the provisions of SFAS No. 157 only with respect to financial assets and liabilities. The adoption of SFAS No. 157 did not have a material effect on the Company s consolidated financial statements for financial assets and liabilities carried at fair value. The Company is currently in the process of evaluating the impact of adopting SFAS No. 157 for non-financial assets and liabilities.

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Valuation techniques used to measure fair value under SFAS No. 157 are required to maximize the use of observable inputs and minimize the use of unobservable inputs. SFAS No. 157 describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs, other than Level 1 prices, such as quoted prices in active markets for similar assets and liabilities, quoted prices for identical or similar assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

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, including certain pricing models, discounted cash flow methodologies and similar techniques.

Unrealized gains and unrealized temporary losses on investments classified as available for sale are included within accumulated other comprehensive (loss) income, net. Upon realization, those amounts are reclassified from accumulated other comprehensive (loss) income, net to gain (loss) on investments, net. Realized gains and losses and other than temporary impairments are reflected in the income statement as gain (loss) on investments, net.

The following table summarizes the composition of the Company s investments at June 30, 2008 and December 31, 2007 (in thousands):

					Classified on Balance Sheet	
		Gross Unrealized			Short-term	Long-term
As of June 30, 2008	Amortized Cost	Gains	Losses	Aggregate Fair Value	Marketable Securities	Marketable Securities
Certificates of deposit	$ 604	$	$	$ 604	$ 604	$
Commercial paper	51,323	12	(119)	51,216	51,216	
U.S. corporate debt securities	139,323	260	(922)	138,661	30,224	108,437
U.S. government agency obligations	110,653	93	(390)	110,356	44,236	66,120
Auction rate securities	295,400		(16,012)	279,388		279,388
	$ 597,303	$ 365	$ (17,443)	$ 580,225	$ 126,280	$ 453,945

					Classified on Balance Sheet	
		Gross Unrealized			Short-term	Long-term
As of December 31, 2007	Amortized Cost	Gains	Losses	Aggregate Fair Value	Marketable Securities	Marketable Securities
Certificates of deposit	$ 835	$	$	$ 835	$ 835	$
Commercial paper	47,669	27	(9)	47,687	47,687	
U.S. corporate debt securities	119,961	305	(423)	119,843	66,190	53,653
U.S. government agency obligations	39,998	118	(1)	40,115	6,429	33,686
Auction rate securities	279,950			279,950	279,950	
	$ 488,413	$ 450	$ (433)	$ 488,430	$ 401,091	$ 87,339

The Company evaluates investments with unrealized losses to determine if the losses are other than temporary. The Company has determined that the gross unrealized losses at June 30, 2008 and December 31, 2007 are temporary. In making this determination, the Company considered the financial condition and near-term prospects of the issuers, the magnitude of the losses compared to the investments cost, the length of time the investments have been in an unrealized loss position and the Company s ability to hold the investments to maturity.

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The following table details the fair value measurements within the fair value hierarchy of the Company s financial assets, including investments and cash equivalents, at June 30, 2008 (in thousands):

	Total Fair Value at June 30, 2008	Fair Value Measurements at Reporting Date Using Level 1	Level 2	Level 3
Money market funds	$ 110,199	$ 110,199	$	$
Certificates of deposit	604	604		
Commercial paper	64,350	64,350		
U.S. government agency obligations	110,356	110,356		
U.S. corporate debt securities	138,661	138,661		
Auction rate securities	279,388			279,388
	$ 703,558	$ 424,170	$	$ 279,388

The following table reflects the activity for the Company s major classes of assets measured at fair value using Level 3 inputs for the six months ended June 30, 2008 (in thousands):

	Auction Rate Securities
Balance as of December 31, 2007	$
Transfers in from Level 2	296,850
Unrealized losses included in accumulated other comprehensive loss	(15,990)
Balance as of March 31, 2008	280,860
Sales of securities	(1,450)
Change in unrealized losses included in accumulated other comprehensive loss	(22)
Balance as of June 30, 2008	$ 279,388

As of June 30, 2008, the Company had grouped money market funds, certificates of deposit, commercial paper, U.S. government agency obligations and U.S. corporate debt securities using a Level 1 valuation because market prices are readily available in active markets. At June 30, 2008, the fair value of the Company s assets grouped using a Level 3 valuation consisted of auction rate securities (ARSs) that are AAA-rated bonds, most of which are collateralized by federally guaranteed student loans. ARSs are long-term variable rate bonds tied to short-term interest rates that may reset through a Dutch auction process that typically occurs every seven to 35 days.

Historically, the carrying value (par value) of the ARSs approximated fair market value due to the resetting of variable interest rates. Beginning in late February 2008 and continuing throughout the period ended June 30, 2008, however, the auctions for ARSs then held by the Company were unsuccessful. As a result, the interest rates on ARSs reset to the maximum rate per the applicable investment offering statements. The Company will not be able to liquidate affected ARSs until a future auction on these investments is successful, a buyer is found outside the auction process, the securities are called or refinanced by the issuer, or the securities mature. Due to these liquidity issues, the Company performed a discounted cash flow analysis to determine the estimated fair value of these investments. The discounted cash flow analysis performed by the Company considered the timing of expected future successful auctions, the impact of extended periods of maximum interest rates, collateralization of underlying security investments and the credit worthiness of the issuer. The discounted cash flow analysis as of June 30, 2008 assumes a weighted average discount rate of 5.5% and expected term of five years. The discount rate was determined using a proxy based upon the current market rates for similar debt offerings within the AAA-rated ARS market. The expected term was based on management s estimate of future liquidity. As a result, as of June 30, 2008, the Company has recorded a cumulative unrealized loss of $16.0 million related to the temporary impairment of the ARSs, which was included in accumulated other comprehensive loss within stockholders equity on the unaudited consolidated balance sheet.

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The Company s investment in ARSs is primarily comprised of student loans that are supported by the federal government as part of the Federal Family Education Loan Program through the United States Department of Education and, to a lesser extent, obligations of municipalities rated single-A or higher. The Company believes the quality of the collateral underlying these securities will enable it to recover the Company s principal balance.

As of December 31, 2007, the Company held $280.0 million of ARSs and classified these as short-term investments. As of June 30, 2008, the Company classified its ARSs as long-term marketable securities on its consolidated balance sheet due to management s estimate of its inability to liquidate these investments within the following twelve months.

In addition, as of June 30, 2008, $3.6 million of the Company s marketable securities were classified as restricted. These securities primarily represent collateral for irrevocable letters of credit in favor of third-party beneficiaries, mostly related to facility leases; $0.1 million of these securities are classified as long-term and $3.5 million are classified as short-term on the unaudited consolidated balance sheet as of June 30, 2008. The restrictions on these marketable securities lapse as the Company fulfills its obligations or as such obligations expire under the terms of the letters of credit. These restrictions are expected to lapse at various times through May 2011.

5. Accounts Receivable

Net accounts receivable consists of the following (in thousands):

	As of June 30, 2008	As of December 31, 2007
Trade accounts receivable	$ 118,165	$ 113,357
Unbilled accounts	15,743	15,978
Gross accounts receivable	133,908	129,335
Allowance for doubtful accounts	(4,840)	(6,878)
Reserve for cash-basis customers	(3,303)	(3,513)
Total accounts receivable reserves	(8,143)	(10,391)
Accounts receivable, net	$ 125,765	$ 118,944

The Company s accounts receivable balance includes unbilled amounts that represent revenues recorded for customers that are typically billed monthly in arrears. The Company records reserves against its accounts receivable balance. These reserves consist of allowances for doubtful accounts and reserves for cash-basis customers. Increases and decreases in the allowance for doubtful accounts are included as a component of general and administrative expenses. The Company s reserve for cash-basis customers increases as services are provided to customers where collection is no longer assured. Increases to the reserve for cash-basis customers are recorded as reductions of revenues. The reserve decreases and revenue is recognized when and if cash payments are received.

Estimates are used in determining these reserves and are based upon the Company s review of outstanding balances on a customer-specific, account-by-account basis. The allowance for doubtful accounts is based upon a review of customer receivables from prior sales with collection issues where the Company no longer believes that the customer has the ability to pay for services previously provided. The Company also performs ongoing credit evaluations of its customers. If such an evaluation indicates that payment is no longer reasonably assured for services provided, any future services provided to that customer will result in the creation of a cash-basis reserve until the Company receives consistent payments. The Company does not have any off-balance sheet credit exposure related to its customers.

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6. Accrued Expenses and Other Current Liabilities

Accrued expenses consist of the following (in thousands):

	As of June 30, 2008	As of December 31, 2007
Payroll and other related benefits	$ 17,010	$ 27,381
Bandwidth and co-location	13,580	12,968
Property, use and other taxes	5,296	10,182
Legal professional fees	1,488	1,781
Other	4,060	3,921
Total	$ 41,434	$ 56,233

7. Net Income per Share

Basic net income per share is computed using the weighted average number of common shares outstanding during the applicable period. Diluted net income per share is computed using the weighted average number of common shares outstanding during the period, plus the dilutive effect of potential common stock. Potential common stock consists of shares issuable pursuant to stock options, deferred stock units, restricted stock units (RSUs) and convertible notes, excluding those options or securities that have an exercise price greater than the average market price for the Company s common stock during the applicable period.

The following table sets forth the components used in the computation of basic and diluted net income per common share for the periods indicated (in thousands, except per share data):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Numerator:				
Net income	$ 34,334	$ 21,646	$ 71,245	$ 40,825
Adjustment for interest expense on assumed conversion of 1% convertible senior notes, net of tax	434	710	860	1,420
Numerator for diluted net income	$ 34,768	$ 22,356	$ 72,105	$ 42,245
Denominator:				
Denominator for basic net income per common share	167,417	164,798	166,688	163,184
Effect of dilutive securities:				
Stock options	4,871	7,372	5,198	7,808
Effect of escrow contingencies	810		810	
Restricted stock units and deferred stock units	1,616	489	1,870	713
Assumed conversion of 1% convertible senior notes	12,927	12,942	12,927	12,943
Denominator for diluted net income per common share	187,641	185,601	187,493	184,648
Basic net income per common share	$ 0.21	$ 0.13	$ 0.43	$ 0.25
Diluted net income per common share	$ 0.19	$ 0.12	$ 0.38	$ 0.23

The Company included 1.1 million shares of common stock issuable under the terms of performance-based RSUs in the computation of diluted net income per share for each of the three and six months ended June 30, 2008, because the performance conditions of these awards had been met as of June 30, 2008. The Company excluded 1.6 million and 0.2 million shares of common stock from the calculation of diluted earnings per share for the three months ended June 30, 2008 and 2007, respectively, and 1.6 million and 0.6 million shares of common stock for the six months ended June 30, 2008 and 2007, respectively, from the calculation of diluted

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earnings per share because the exercise prices of stock options issuable in respect of such numbers of shares were greater than the average market price of the Company s common stock during the respective periods. Additionally, 2.6 million and 3.6 million shares issuable in respect of performance-based RSUs were excluded from the computation of diluted net income per share for the three and six months ended June 30, 2008 and 2007 because the performance conditions had not been met as of June 30, 2008 and 2007, respectively.

The calculation of assumed proceeds used to determine the diluted weighted average shares outstanding under the treasury stock method in the periods presented was adjusted by tax windfalls and shortfalls associated with all of the Company s outstanding stock awards. Such windfalls and shortfalls are computed by comparing the tax deductible amount of outstanding stock awards to their grant date fair values and multiplying the results by the applicable statutory tax rate. A positive result creates a windfall, which increases the assumed proceeds, and a negative result creates a shortfall, which reduces the assumed proceeds.

8. Stockholders Equity

Stock-Based Compensation Expense

The following table summarizes the components of total stock-based compensation expense included in the Company s condensed consolidated statements of operations for the three and six months ended June 30, 2008 and 2007 (in thousands):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Stock-based compensation expense by type of award:				
Stock options	$ 5,468	$ 8,032	$ 11,640	$ 14,714
Deferred stock units	1,885	925	1,885	925
Restricted stock units	10,667	8,725	16,454	19,351
Shares issued under the Employee Stock Purchase Plan	897	953	1,860	1,859