VIALTA INC
Form 10-Q
August 13, 2003

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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, 2003.

OR

[ ] Transitional Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the transition period from: ___________ to: __________ .

Commission file number 0-32809

VIALTA, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

Delaware	94-3337236
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

48461 Fremont Boulevard
Fremont, California 94538
(Address, including zip code, of Registrant s principal executive offices)

(510) 870-3088
(Registrant s telephone number, including area code)

Indicate by check 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 is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [X]

The number of outstanding shares of the registrant s common stock, par value $0.001 per share, on August 7, 2003 was 82,193,391 shares.

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VIALTA, INC.

FORM 10-Q: QUARTER ENDED JUNE 30, 2003

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PART I. FINANCIAL INFORMATION

ITEM 1: Financial Statements

VIALTA, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)
(unaudited)

	June 30, 2003	December 31, 2002
Assets		
Current assets:		
Cash and cash equivalents	$ 22,752	$ 21,863
Short-term investments	7,509	10,838
Accounts receivable, net	618	1,362
Inventories	3,010	2,834
Prepaid expenses and other	653	1,253
Total current assets	34,542	38,150
Property and equipment, net	1,322	2,132
Other assets	29	45
Total assets	$ 35,893	$ 40,327
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 929	$ 1,164
Accrued liabilities and other	2,327	3,555
Deferred profit	1,627	3,230
Total current liabilities	4,883	7,949
Stockholders equity:		
Common stock	94	94
Additional paid-in capital	144,112	144,105
Treasury stock	(9,458)	(9,163)
Accumulated deficit	(103,744)	(102,666)
Accumulated other comprehensive income	6	8
Total stockholders equity	31,010	32,378
Total liabilities and stockholders equity	$ 35,893	$ 40,327

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

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VIALTA, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2003	**2002**	**2003**	**2002**
Net revenue	$ 2,520	$	$ 6,363	$
Cost of goods sold	570		1,433	
Gross profit	1,950		4,930	
Operating expenses:				
Product costs		1,137		1,137
Engineering and development	621	3,981	1,589	8,204
Sales and marketing	641	732	1,083	1,346
General and administrative	1,974	1,427	3,704	3,239
Amortization and impairment of content licenses		947		1,200
Total operating expenses	3,236	8,224	6,376	15,126
Operating loss	(1,286)	(8,224)	(1,446)	(15,126)
Interest income and other, net	178	360	366	723
Net loss	$ (1,108)	$ (7,864)	$ (1,080)	$ (14,403)
Net loss per share:				
Basic and diluted	$ (0.01)	$ (0.09)	$ (0.01)	$ (0.17)
Weighted average common shares outstanding:				
Basic and diluted	82,151	83,752	82,194	84,492

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

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Six months ended June 30, 2003	Six months ended June 30, 2002
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (1,080)	$ (14,403)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	1,016	3,495
Amortization and impairment of content licenses		1,200
Write-down of long-term investment		39
Changes in operating assets and liabilities:		
Accounts receivable, net	744	
Related party receivable/payables, net	443	113
Inventories	(176)	
Prepaid expenses and other	616	(59)
Restricted cash		(1,738)
Deferred profit	(1,603)	
Accounts payable and accrued liabilities and other	(1,906)	843
Net cash used in operating activities	(1,946)	(10,510)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of short-term investments	(7,478)	2,483
Proceeds from sales of short-term investments	10,807	
Purchase of content licenses		(10,043)
Acquisitions of property and equipment	(206)	(166)
Net cash provided by (used in) investing activities:	3,123	(7,726)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Issuance of shares of common stock	7	14
Repurchases of shares of common stock	(295)	(3,481)
Net cash used in financing activities:	(288)	(3,467)
Net increase (decrease) in cash and cash equivalents	889	(21,703)
Cash and cash equivalents, beginning of the period	21,863	61,886
Cash and cash equivalents, end of the period	$ 22,752	$ 40,183

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

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VIALTA, INC.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1. THE COMPANY

We were incorporated in California in April 1999 and reincorporated in the State of Delaware in May 2001.

We develop, design and market consumer electronics products designed to maximize the advantages of digital technology in a convenient and easy-to-use manner. Our newest product, Beamer , is a personal videophone. Beamer adds color video to phone calls, enabling Beamer users to see the person they are calling. Beamer works with any home phone over any standard (analog) home phone line, and at no additional cost to a regular phone call. Beamers are primarily sold in pairs, since the party receiving the video call must also have a Beamer (or compatible videophone). We began nationwide retail distribution of Beamer during the third quarter of 2002, and it is currently carried by retailers such as Best Buy, Fry s Electronics, The Good Guys, The Sharper Image and Frontgate. The first product we developed was ViDVD, a multimedia DVD player that offered additional features such as CD, MP3 and karaoke disc playback, Internet connectivity and the ability to view digital photographs. We are currently not marketing the ViDVD. We also developed ViMagazine, a proprietary, encrypted, magazine-style DVD-format disc, which is capable of delivering a wide variety of entertainment, from feature films to children s programming, music and other programming content to be used exclusively in conjunction with our ViDVD. As a result of our decision not to continue marketing ViDVD, we have not introduced ViMagazine.

Since our inception, we have incurred substantial losses and negative cash flows from operations. We expect operating losses and negative cash flows from operations to continue for the foreseeable future and anticipate that losses may increase from current levels because of additional costs and expenses related to sales and marketing activities, continued expansion of operations, expansion of product offerings and development of relationships with other businesses. We believe that we have sufficient cash and cash equivalents and short-term investments to fund our operations through June 30, 2004. However, in the longer term, failure to generate sufficient revenues, raise additional capital or reduce spending could have a material adverse effect on our ability to achieve our intended business objectives.

From our inception through December 31, 2002, we were a development stage enterprise. During the first quarter of 2003, we commenced principal operations and are no longer classified as a development stage company.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared by us pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the accompanying unaudited condensed interim financial statements contain all adjustments, all of which are normal and recurring in nature, necessary to fairly present our financial position, operating results and cash flows. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2002, included in our Annual Report on Form 10-K filed on March 28, 2003. The results of operations for the three and six months ended June 30, 2003 are not necessarily indicative of the results that may be expected for any other period or for the fiscal year ending December 31, 2003.

Reclassifications

Certain prior year amounts in the condensed consolidated financial statements and the notes hereto have been reclassified where necessary to conform to the quarter ended June 30, 2003.

Principles of consolidation

The consolidated financial statements include the accounts of Vialta and our subsidiaries. All material intercompany accounts and transactions have been eliminated in consolidation.

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Cash equivalents and investments

We consider all highly liquid investments with an initial maturity of 90 days or less to be cash equivalents. Cash equivalents primarily represent money market funds.

Short-term investments are comprised primarily of debt instruments that have been classified as available-for-sale. Management determines the appropriate classification of securities at the time of purchase and re-evaluates the classification at each reporting date. Marketable equity and debt securities are carried at their fair market value based on quoted market prices as of the balance sheet date. Realized gains or losses are determined on the specific identification method and are reflected in income. Net unrealized gains or losses are recorded directly in stockholders equity except those unrealized losses that are deemed to be other than temporary, which are reflected in investment losses.

Revenue recognition

We generally recognize revenue on products sold to end customers upon shipment provided that we have no post-sale obligations, we can reliably estimate and accrue warranty costs and sales returns, the price is fixed or determinable and collection of the resulting receivable is reasonably assured. For sales to end customers that do not meet the above criteria, revenue is deferred until such criteria are met.

Products sold to retailers and distributors are subject to rights of return. We defer recognition of revenue on products sold to retailers and distributors until the retailers and distributors sell the products to their customers. We recognize revenue from retailers and distributors according to information on shipments to their customers as provided by those retailers and distributors. If information on shipments to their customers is not provided in a timely and accurate manner, there may be a material impact on our reported results of operations and financial condition. Revenue is also deferred for the initial thirty-day period during which our direct customers, retailers and distributors have the unconditional right to return products.

Revenue for the three and six months ended June 30, 2003 was $2.5 million and $6.4 million, respectively. There was no revenue for the three and six months ended June 30, 2002. During the first quarter of 2003, we began to recognize revenue on sales of Beamer, net of estimated warranty claims and returns. We began nationwide distribution of Beamer during the third quarter of 2002 and experienced more significant shipments during the fourth quarter of 2002. For most of these shipments, the standard warranty period had not been completed as of December 31, 2002. Due to a limited history of warranty and sales returns for Beamer, we did not recognize revenue from sales through December 31, 2002. As a result, revenue for the six months ended June 30, 2003 includes the recognition of deferred revenue of approximately $2.8 million related to shipments of Beamer which were made during the third and fourth quarters of 2002.

Allowances for sales returns

Allowances are provided for estimated returns. Provision for return allowances are recorded at the time when revenue is recognized based on historical returns, current economic trends and changes in customer demand. Such allowances are adjusted periodically to reflect actual experience and anticipated returns.

Warranty

We provide a limited warranty on our products for periods ranging from 90 days to 12 months from the date of sale to the end customers. We estimate warranty costs based on historical experience and accrue for estimated costs as a charge to cost of sales when revenue is recognized. During the six months ended June 30, 2003, warranty costs did not have a material impact on our reported results of operations and financial condition. In the future, actual warranty costs may be higher than our estimates.

Comprehensive income (loss)

Comprehensive income (loss) is defined to include all changes in equity during a period from non-owner sources. For the three and six months ended June 30, 2003, comprehensive income (loss) approximated the net losses reported. The difference between net loss and comprehensive loss for the three months and six months ended June 30, 2002 was approximately $14,000 and $104,000, respectively, which related to unrealized losses on available-for-sale investments. Comprehensive loss for the three months and six months ended June 30, 2002 was approximately $7.9 and $14.5 million, respectively.

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Stock-based compensation

We account for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25, or APB No. 25, Accounting for Stock Issued to Employees. Under APB No. 25, compensation cost is measured as the excess, if any, of the quoted market price of its stock at the date of grant over the exercise price of the option granted. Compensation cost for stock options, if any, is recognized ratably over the vesting period. We provide additional pro forma disclosures as required under SFAS No. 123, Accounting for Stock-Based Compensation and SFAS No. 148, Accounting for Stock-Based Compensation, Transition and Disclosure.

The following table illustrates the effect on our net loss and net loss per share if we had recorded compensation costs based on the estimated grant date fair value as defined by SFAS No. 123 for all granted stock-based awards (in thousands, except per share amounts).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Net loss, as reported	$(1,108)	$(7,864)	$(1,080)	$(14,403)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(390)	(897)	(739)	(1,947)
Pro forma net loss	$(1,498)	$(8,761)	$(1,819)	$(16,350)
Pro forma net loss per share:				
Basic and diluted	$ (0.02)	$ (0.10)	$ (0.02)	$ (0.19)

NOTE 3. RELATED PARTY TRANSACTIONS

The following is a summary of major transactions between us and ESS Technology, Inc., which was formerly our parent company, for the periods presented (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Net receivables (payables) at beginning of period	$ (12)	$ 99	$ (33)	$ 64
Charges by Vialta to ESS:				
Administrative & management service fees		99		202
Other		(190)	2	14
Charges by ESS to Vialta:				
Administrative & management service fees	(20)	(49)	(52)	(137)
Purchase of products	(15)	(53)	(19)	(69)
Building lease	(464)	(463)	(927)	(926)
Cash receipts from ESS	(1)	(153)	(2)	(338)
Cash payments made to ESS	36	661	555	1,141
Net receivables (payables) at end of period	$(476)	$ (49)	$(476)	$ (49)

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NOTE 4. INVENTORIES

The following table summarizes the activity in Beamer related inventories and reserves for the six months ended June 30, 2003 (in thousands):

	Beamer		
	Gross	Reserve	Net
As of December 31, 2002	$11,866	$(9,032)	$2,834
Purchase of inventories	553		553
Shipments, net	(903)	629	(274)
Use or Disposal of inventories	(311)	143	(168)
As of March 31, 2003	11,205	(8,260)	2,945
Purchase of inventories	1,020		1,020
Shipments, net	(1,903)	1,374	(529)
Use or Disposal of inventories	(152)	(274)	(426)
As of June 30, 2003	$10,170	$(7,160)	$3,010
Raw material	$		