

Virgin Mobile USA, Inc.
Form 10-Q
November 16, 2007
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2007

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: 001-33735

Virgin Mobile USA, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of

incorporation or organization)

20-8826316
(I.R.S. Employer

Identification No.)

10 Independence Boulevard, Warren, New Jersey

07059

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(Address of principal executive offices)

(908) 607-4000

(Zip Code)

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

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

Large accelerated filer Accelerated filer Non-accelerated filer

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

The number of shares of each of the registrant's classes of common stock outstanding as of November 9, 2007 was as follows:

Class A common stock, par value \$0.01 per share	53,146,052
Class B common stock, par value \$0.01 per share	1
Class C common stock, par value \$0.01 per share	115,062

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

Virgin Mobile USA, Inc.

Condensed Balance Sheet

(Unaudited)

As of September 30, 2007

Assets	
Current assets:	
Cash and cash equivalents	\$ 1
Total assets	\$ 1
Commitments and contingencies	
Stockholder s Equity	
Common Stock; \$0.01 par value, 100 shares authorized, 1 share issued and outstanding	\$ 1
Additional paid-in-capital	1
Total stockholder s equity	\$ 1

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

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Virgin Mobile USA, Inc.

Notes to the Condensed Balance Sheet (Unaudited)

1. Description of Business and Basis of Presentation

Virgin Mobile USA, Inc. (the Company), a Delaware corporation was formed on April 11, 2007 and capitalized on April 17, 2007 in connection with a proposed initial public offering.

Basis of Presentation

The accompanying unaudited balance sheet of the Company has been prepared in accordance with accounting principles generally accepted in the United States of America and Article 10 of Regulation S-X of the Securities and Exchange Commission (SEC). Accordingly, it does not include annual disclosures necessary for a presentation of the Company's financial position in conformity with accounting principles generally accepted in the United States of America. In the opinion of management, the interim financial information provided herein reflects all adjustments (consisting of normal and recurring adjustments) necessary for a fair presentation of the Company's financial position for the interim periods presented on a basis consistent with the Company's historical audited balance sheet and the accompanying notes. This document should be read in conjunction with the financial statements and accompanying notes included in the Company's prospectus dated October 10, 2007 and filed with the SEC on October 11, 2007.

2. Subsequent Events

Reorganization and Initial Public Offering

In connection with its initial public offering (IPO), the Company, Virgin Mobile USA, LLC and Bluebottle USA Investments L.P. and its subsidiaries (Investments) completed a reorganization. As part of the reorganization, Virgin Mobile USA, LLC converted to a limited partnership and changed its name to Virgin Mobile USA, L.P. (the Operating Partnership). Upon completion of the reorganization and the IPO, the equity, on a converted basis, in the Company's business was owned 35.1% by Corvina Holdings Limited and Cortaire Limited, affiliates of Virgin Group Holdings Limited, (the Virgin Group), 18.5% by Sprint Ventures, Inc., an affiliate of Sprint Nextel Corporation together with its affiliated entities (Sprint Nextel), through its ownership in the Operating Partnership, 4.2% by other minority investors and the remaining 42.2% is publicly traded on the New York Stock Exchange.

On October 16, 2007, the Company completed its IPO and the Company and the selling stockholders sold 27,500,000 shares of Class A Common Stock. The Company received net proceeds of \$355.4 million, after deducting underwriting commissions and discounts of \$23.7 million and estimated offering expenses of \$4.6 million. The Company used \$136 million of the IPO proceeds to pay Sprint Nextel for a portion of Sprint Nextel's limited liability company interests in Virgin Mobile USA, LLC that the Company purchased in connection with the reorganization and the IPO. The remaining net proceeds of \$219.4 million were contributed to the Operating Partnership through Investments and Bluebottle USA Holdings L.P. (Holdings). Holdings used these proceeds to purchase additional limited partnership units in the Operating Partnership. The Operating Partnership used the proceeds to (1) repay \$150 million of outstanding borrowings and \$0.8 million of accrued interest under the senior secured credit facility and (2) repay \$45 million of indebtedness and \$0.6 million of accrued interest owed to Sprint Nextel under the subordinated secured revolving credit facility. Subsequent to the IPO, the Operating Partnership used the remaining net proceeds of approximately \$23.1 million for general corporate purposes.

Following the reorganization and the IPO, the authorized capital stock of the Company consists of: (i) Class A common stock, entitled to one vote per share on all matters submitted to a vote of stockholders; (ii) one share of Class B common stock (presently held by Sprint Nextel) entitled to a number of votes per share on all matters submitted to a vote of stockholders that is equal to the total number of shares of Class A common stock for which the partnership units that Sprint Nextel holds in the Operating Partnership are exchangeable; (iii) Class C common stock (presently held by the Virgin Group) entitled to one vote per share on all matters submitted to a vote of stockholders and convertible into Class A common stock on a one-for-one basis at any time; and (iv) preferred stock. Sprint Nextel and the Virgin Group, the principal stockholders, are able to exercise control over the Company's management and affairs and all matters requiring stockholder approval as a result of their ownership of 35.1% voting power in Virgin Mobile USA, Inc. (in the form of Class A common stock and Class C common stock) in the case of the Virgin Group and of 18.5% voting power (in the form of Class B common stock) in the case of Sprint Nextel. Immediately following the reorganization and the IPO, the Company had the following classes of capital stock authorized, and issued and outstanding.

Table of Contents**Virgin Mobile USA, Inc.****Notes to the Condensed Balance Sheet (Unaudited)**

	Shares Authorized	Shares Issued and Outstanding
Class A	200,000,000	53,022,034
Class B	1	1
Class C	999,999	115,062
Preferred Stock(1)		

(1) The Company's certificate of incorporation authorizes the board of directors to establish one or more series of preferred stock (including convertible preferred stock). No shares of preferred stock were outstanding.

In its December 31, 2007 financial statements, the Company will account for the reorganization transactions, for all periods presented, using a carryover basis, similar to a pooling-of-interest as the reorganization transactions were premised on a non-substantive exchange in order to facilitate the IPO. This is consistent with Financial Accounting Standards Board Technical Bulletin 85-5, Issues Relating to Accounting for Business Combinations, including Costs of Closing Duplicate Facilities of an Acquirer; Stock Transactions between Companies under Common Control; Down-Stream Mergers, Identical Common Shares for a Pooling of Interests; and Pooling of Interests by Mutual and Cooperative Enterprises.

Pro Forma Balance Sheet Information (Unaudited)

The unaudited pro forma balance sheet data below reflects the transactions noted above that occurred subsequent to September 30, 2007. The pro forma balance sheet gives effect to (1) the reorganization transactions, including the consolidation of the Company, Virgin Mobile USA, L.P. and Investments on a carryover basis, (2) receipt of \$355.4 million of net proceeds from the IPO, (3) payment of \$136 million to Sprint Nextel for limited liability company interests in Virgin Mobile USA, LLC purchased by the Company, (4) repayment of \$150 million of outstanding borrowings and \$0.8 million of accrued interest under the senior secured credit facility, and (5) repayment of \$45 million of indebtedness and \$0.6 million of accrued interest owed to Sprint Nextel under the subordinated revolving credit facility, as if these transactions had occurred on September 30, 2007. Sprint Nextel's 18.5% interest in the Operating Partnership is reflected as minority interest in the unaudited pro forma balance sheet.

Table of Contents**Virgin Mobile USA, Inc.****Notes to the Condensed Balance Sheet (Unaudited)****Pro Forma Condensed Consolidated Balance Sheet****(Unaudited)****(In thousands)**

	September 30, 2007
Assets	
Current assets:	
Cash and cash equivalents	\$ 23,106
Other current assets	226,902
Total current assets	250,008
Property and equipment, net	45,321
Other assets	11,285
Total assets	\$ 306,614
Liabilities and stockholders / members equity	
Current liabilities:	
Current portion of long-term debt	\$ 31,988
Other current liabilities	378,729
Total current liabilities	410,717
Other liabilities	5,585
Long-term debt	250,762
Related party debt	45,000
Total non-current liabilities	301,347
Minority interest	(115,447)
Total stockholders deficit	(290,003)
Total liabilities and stockholders deficit	\$ 306,614

The unaudited pro forma balance sheet does not reflect any adjustments relating to tax receivable agreements with Sprint Nextel and the Virgin Group, discussed below, except for adjustments relating to the initial sale of limited liability company interests by Sprint Nextel to the Company as part of the reorganization transactions, since the amount and timing of the utilization of the tax benefits under those agreements is unknown. However, any payments to Sprint Nextel and the Virgin Group pursuant to their respective tax receivable agreements are expected to be accounted for as follows:

the Company will recognize a deferred tax asset relating to the increase in the tax bases of the assets owned, in the case of the tax receivable agreement with Sprint Nextel based on enacted tax rates at the date of the transactions giving rise to the increased tax bases;

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the Company will evaluate the likelihood of realizing the benefits of such deferred tax asset and reduce the deferred tax asset with a valuation allowance if there is a more likely than not chance that the deferred tax asset will not be realized; and

the Company will record a liability for the amount expected to be paid under the tax receivable agreement with Sprint Nextel or the tax receivable agreement with the Virgin Group, as the case may be, estimated using assumptions consistent with those used in estimating the Company's ability to realize net deferred tax assets.

Table of Contents**Virgin Mobile USA, Inc.****Notes to the Condensed Balance Sheet (Unaudited)****Pro Forma Earnings Per Share (Unaudited)**

The calculation of pro forma basic and diluted earnings/(loss) per share converts the historical weighted average number of units of limited liability company interests in Virgin Mobile USA, LLC outstanding as of September 30, 2007 and 2006 to common stock based on a conversion rate used in the reorganization. New equity issued in the IPO was not outstanding on September 30, 2007 and therefore not included in weighted average shares for any period. The net (loss)/income of Virgin Mobile USA, LLC and Investments is combined and the equity in income/(loss) of investee is eliminated in determining the pro forma net (loss)/income. Pro forma net (loss)/income per share is calculated by dividing the pro forma net (loss)/income per share by the pro forma historical weighted average number of shares of common stock outstanding for each period shown. The Company's pro forma net (loss) for the three months ended September 30, 2007 and 2006, and accordingly the diluted (loss) per share is the same as the basic (loss) per share for that period, as any potentially dilutive securities would reduce the net loss per share.

	Three months ended September 30, 2007		Nine months ended September 30, 2007	
	Basic	Diluted	Basic	Diluted
(In thousands, except per share amounts) (Unaudited)				
Pro forma weighted average shares outstanding:				
Common stock (i)	49,352	49,352	49,098	49,098
Stock options - Class A common stock (ii)				1,004
Restricted stock units - Class A common stock (iii)				19
Pro forma weighted average shares outstanding	49,352	49,352	49,098	50,121
Pro forma net (loss)/income:				
Virgin Mobile USA, LLC	\$ (7,301)	\$ (7,301)	\$ 19,215	\$ 19,215
Bluebottle USA Investments L.P	(3,523)	(3,523)	8,775	8,775
Virgin Mobile USA, Inc.				
Eliminate equity in loss/(income) of investee (iv)	3,443	3,443	(9,060)	(9,060)
Pro forma net (loss)/income	\$ (7,381)	\$ (7,381)	\$ 18,930	\$ 18,930
Pro forma net (loss)/income per common share	\$ (0.15)	\$ (0.15)	\$ 0.39	\$ 0.38
	Three months ended September 30, 2006		Nine months ended September 30, 2006	
	Basic	Diluted	Basic	Diluted
(In thousands, except per share amounts) (Unaudited)				
Pro forma weighted average shares outstanding:				
Common stock (i)	48,413	48,413	48,408	48,408
Stock options - Class A common stock (ii)				453
Restricted stock units - Class A common stock (iii)				
Pro forma weighted average shares outstanding	48,413	48,413	48,408	48,861
Pro forma net (loss)/income:				
Virgin Mobile USA, LLC	\$ (5,062)	\$ (5,062)	\$ 8,055	\$ 8,055

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Bluebottle USA Investments L.P	(2,399)	(2,399)	3,711	3,711
Virgin Mobile USA, Inc.				
Eliminate equity in loss/(income) of investee (iv)	2,386	2,386	(3,799)	(3,799)
Pro forma net (loss)/income	\$ (5,075)	\$ (5,075)	\$ 7,967	\$ 7,967
 Pro forma net (loss)/income per common share	 \$ (0.10)	 \$ (0.10)	 \$ 0.16	 \$ 0.16

(i) Represents weighted average number of units of limited liability company interests in Virgin Mobile USA, LLC for the period converted to weighted average common shares based on a conversion rate used in the reorganization.

Table of Contents**Virgin Mobile USA, Inc.****Notes to the Condensed Balance Sheet (Unaudited)**

(ii) The issuance of options on shares of Class A common stock to holders of awards granted under the 2005 Stock Appreciation Rights Plan and the conversion of units granted under the 2002 and 2006 Stock Appreciation Rights Plans (2002 and 2006 SAR Plans) into options on shares of the Company's Class A common stock has been included in the computation of diluted pro forma earnings per share using the treasury stock method. For the three months ended September 30, 2007 and 2006, approximately 554,000 and approximately 642,000 options were excluded from the calculation of diluted earnings/(loss) per share since the effect was anti-dilutive.

(iii) The Restricted Stock Unit (RSU) Awards granted on February 14, 2007 and May 23, 2007 are included in the computation of diluted pro forma earnings per share using the treasury stock method assuming a conversion to Class A common shares.

(iv) Investments accounts for its share of Virgin Mobile USA, LLC under the equity method of accounting, as it does not control the operations of Virgin Mobile USA, LLC. Under the equity method, Investments adjusts its investment account for its proportionate share of Virgin Mobile USA, LLC's net income or loss in equity in loss/(income) of investee.

Share-Based Awards

On October 10, 2007, the Company's Board of Directors approved the Virgin Mobile USA, Inc. 2007 Omnibus Incentive Compensation Plan (the 2007 Omnibus Share Plan). The 2007 Omnibus Share Plan provides for the grant of equity-based awards, including stock options, restricted stock, performance shares, stock appreciation rights, common stock, performance units or cash based awards, as determined by the Company's Compensation Committee. Up to 7.7 million shares were authorized for issuance under the 2007 Omnibus Share Plan, including shares that underlie awards originally made under the Virgin Mobile USA, LLC equity-based incentive plans.

In connection with the IPO, all awards outstanding under the Virgin Mobile USA, LLC Option Plans and Agreements and the 2002 and 2006 SAR Plans were converted into non-qualified stock options of the Company, exercisable for shares of the Company's Class A common stock. All awards outstanding under the Virgin Mobile USA, LLC 2007 Restricted Stock Unit Plan were converted into shares of the Company's Class A Restricted Stock. All vesting provisions and maximum terms under the various plans were unchanged, and all accrued liabilities were transferred from Virgin Mobile USA, LLC to the Company and recorded in additional paid-in-capital. The following table summarizes the share-based awards converted upon completion of the IPO:

	Operating Partnership Awards Converted to VMU Inc. Awards	
	Number	Number
	of pre-IPO	of post-IPO
	Awards Outstanding	Awards Outstanding
2002 SAR Awards	47	20,244
2006 SAR Awards	1,666	710,925
Non-Qualified Options	6,115	2,609,662
2007 RSU Awards	1,191	508,307
Total	9,019	3,849,138

Under the 2007 Omnibus Share Plan, concurrent with the IPO, the Company issued Restricted Stock Unit (RSU) awards to certain employees of the Operating Partnership, which vest ratably over two years, and non-qualified stock option awards to holders of the Virgin Mobile USA, LLC's 2005 Stock Appreciation Rights Plan awards, which vest ratably over four years. In addition, the Company made its on going long-term incentive awards to eligible employees of the Operating Partnership, in the form of RSU awards and non-qualified stock option awards, all of which vest ratably over approximately 3.75 years. In addition, the Company issued RSU awards to non-employee members of the Board of

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Directors, which vest ratably over four years. The exercise price of the stock options issued, as well as the fair value of the RSU awards issued, equals the initial public offering price of \$15.00. The fair value of the stock options issued was estimated as of the grant date based on the Black-Scholes option pricing model (the Black-Scholes model) as discussed below.

Table of Contents**Virgin Mobile USA, Inc.****Notes to the Condensed Balance Sheet (Unaudited)**

The following table summarizes the equity-based awards granted upon IPO:

	Awards Granted	Fair Value per Award
	at IPO	
RSU Awards		
IPO RSU Grant	561,169	\$ 15.00
Annual RSU Grant	216,367	15.00
Board of Directors RSU Grant	31,998	15.00
Total RSU Awards	809,534	
Option Awards		
IPO Option Grant	256,284	\$ 6.70
Annual Option Grant	1,006,121	6.70
Total Option Awards	1,262,405	
Total Awards	2,071,939	

Immediately following these conversions and new grants, there were approximately 1.8 million shares available for future grants under the 2007 Omnibus Share Plan.

The Company's significant accounting policies related to its Share-Based Award Programs are as follows:

The Company accounts for its share-based awards in accordance with SFAS No. 123R, *Share Based Payment* (SFAS 123R), which requires the Company to recognize expense for the value of its share-based award compensation over the relevant service period, which is generally the vesting period.

The Company's option and RSU awards are classified as equity awards. The Company elected to amortize the fair value of its share-based awards on a straight-line basis over the requisite service period, which is generally the vesting period.

Valuation of Awards

The fair value of RSU awards issued was the fair market value of the Company's Class A common stock on the date of grant. The fair value of option awards issued was estimated as of the grant date based on the Black-Scholes model. The Black-Scholes model takes into account the exercise price and expected life of the award, the current value and expected volatility of the underlying units, expected dividends and the risk-free interest rate for the expected term of the award. Judgment was required in determining certain inputs to the model.

The following assumptions were used for the Black-Scholes model to value the Company's option awards at grant date:

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Expected volatility	51.63%
Expected life	4.0 years
Expected dividend yield	0.00%
Risk-free interest rate	4.29