

SEACHANGE INTERNATIONAL INC

Form 10-Q

June 09, 2008

[Table of Contents](#)

## 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 April 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: 0-21393

## SEACHANGE INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

**Delaware**  
(State or other jurisdiction of

**04-3197974**  
(IRS Employer

incorporation or organization)

Identification No.)

**50 Nagog Park, Acton, MA 01720**

(Address of principal executive offices, including zip code)

**Registrant's telephone number, including area code: (978) 897-0100**

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

The number of shares outstanding of the registrant's Common Stock on June 5, 2008 was 30,819,896.

---

**Table of Contents**

**SEACHANGE INTERNATIONAL, INC.**

**Table of Contents**

	<b>Page</b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
Item 1. <u>Unaudited Financial Statements</u>	
<u>Condensed Consolidated Balance Sheets at April 30, 2008 and January 31, 2008</u>	3
<u>Condensed Consolidated Statements of Operations for the three months ended April 30, 2008 and April 30, 2007</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the three months ended April 30, 2008 and April 30, 2007</u>	5
<u>Notes to Condensed Consolidated Financial Statements</u>	6-14
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	14-23
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	23
Item 4. <u>Controls and Procedures</u>	24
<b><u>PART II. OTHER INFORMATION</u></b>	
Item 1. <u>Legal Proceedings</u>	25
Item 1A. <u>Risk Factors</u>	26
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	26
Item 6. <u>Exhibits</u>	26
<u>SIGNATURES</u>	27

**Table of Contents****PART I FINANCIAL INFORMATION****ITEM 1. Financial Statements****SEACHANGE INTERNATIONAL, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS***(in thousands, except share data)*

	<b>April 30, 2008 (unaudited)</b>	<b>January 31, 2008</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 52,147	\$ 63,359
Marketable securities	20,065	19,266
Accounts receivable, net of allowance for doubtful accounts of \$870 at April 30, 2008 and \$799 at January 31, 2008,	42,629	28,376
Unbilled receivables	5,950	7,367
Inventories, net	16,626	14,315
Prepaid expenses and other current assets	3,265	2,656
<b>Total current assets</b>	<b>140,682</b>	<b>135,339</b>
Property and equipment, net	27,491	28,066
Marketable securities	6,749	5,272
Investments in affiliates	13,227	12,668
Intangible assets, net	6,317	6,809
Goodwill	29,398	29,471
Other assets	322	271
<b>Total assets</b>	<b>\$ 224,186</b>	<b>\$ 217,896</b>
<b>Liabilities and Stockholders Equity</b>		
Current liabilities:		
Accounts payable	\$ 12,172	\$ 9,636
Income taxes payable	585	1,625
Other accrued expenses	8,915	17,387
Customer deposits	1,152	1,259
Deferred revenues	24,685	19,103
Deferred tax liabilities	92	93
<b>Total current liabilities</b>	<b>47,601</b>	<b>49,103</b>
Distribution and losses in excess of investment	1,746	1,458
Deferred tax liabilities and income taxes payable	2,060	1,933
<b>Total liabilities</b>	<b>51,407</b>	<b>52,494</b>
Commitments and contingencies (Note 6)		
Stockholders equity:		
Convertible preferred stock, \$0.01 par value; 5,000,000 shares authorized, none issued or outstanding		
Common stock, \$0.01 par value; 30,867,640 and 29,904,311 shares issued and outstanding at April 30, 2008 and January 31, 2008 respectively	312	299

## Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

Additional paid-in capital	200,920	191,627
Treasury Stock, at cost 322,459 and 39,784 shares at April 30, 2008 and January 31, 2008, respectively	(1,982)	
Accumulated deficit	(28,404)	(28,747)
Accumulated other comprehensive income	1,933	2,223
Total stockholders' equity	172,779	165,402
Total liabilities and stockholders' equity	\$ 224,186	\$ 217,896

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

**Table of Contents****SEACHANGE INTERNATIONAL, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS***(in thousands, except share data)**(unaudited)*

	<b>Three Months Ended April 30, 2008</b>	<b>April 30, 2007</b>
Revenues:		
Product	\$ 26,994	\$ 20,928
Services	18,390	17,916
	45,384	38,844
Cost of revenues:		
Product	10,725	9,362
Services	11,897	11,665
	22,622	21,027
Gross profit	22,762	17,817
Operating expenses:		
Research and development	10,476	10,337
Selling and marketing	6,423	5,785
General and administrative	5,111	4,903
Amortization of intangibles	396	797
	22,406	21,822
Income (loss) from operations	356	(4,005)
Interest and other income, net	695	467
Income (loss) before income taxes and equity income in earnings of affiliates	1,051	(3,538)
Income tax expense	(425)	(1,263)
Equity (loss) income in earnings of affiliates, net of tax	(283)	218
Net income (loss)	\$ 343	\$ (4,583)
Earnings (loss) per share:		
Basic	\$ 0.01	\$ (0.16)
Diluted	\$ 0.01	\$ (0.16)
Weighted average common shares outstanding:		
Basic	30,477	29,389
Diluted	30,817	29,389

Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

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

**Table of Contents****SEACHANGE INTERNATIONAL, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS***(in thousands)**(unaudited)*

	<b>Three Months Ended</b>	
	<b>April 30,</b>	<b>April 30,</b>
	<b>2008</b>	<b>2007</b>
Net income (loss)	\$ 343	\$ (4,583)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation	1,728	2,030
Amortization of intangibles and capitalized software	588	1,156
Inventory valuation charge	260	274
Allowance for doubtful accounts receivable	70	75
Discounts earned and amortization of premiums on marketable securities	15	(25)
Equity loss (income) in earnings of affiliates	283	(218)
Stock-based compensation	869	751
Deferred income taxes	121	794
Changes in operating assets and liabilities:		
Accounts receivable	(14,676)	1,146
Unbilled receivables	1,417	(923)
Inventories	(3,011)	(2,340)
Income taxes receivable	35	26
Prepaid expenses and other assets	(789)	(1,117)
Accounts payable	(384)	377
Income taxes payable	713	438
Accrued expenses	(372)	730
Customer deposits	(107)	5,660
Deferred revenues	5,583	(2,260)
Other	21	(4)
Net cash (used in) provided by operating activities	(7,293)	1,987
<b>Cash flows from investing activities:</b>		
Purchases of property and equipment	(715)	(875)
Proceeds from sale of property and equipment		468
Purchases of marketable securities	(11,355)	(7,723)
Proceeds from sale and maturity of marketable securities	9,974	12,183
Acquisition of businesses and payment of contingent consideration		(154)
Capital distribution from investment in affiliate	(227)	869
Net cash (used in) provided by investing activities	(2,323)	4,768
<b>Cash flows from financing activities:</b>		
Purchase of treasury stock	(1,823)	
Proceeds from issuance of common stock	330	136
Net cash provided by financing activities	(1,493)	136
Effect of exchange rates on cash	(103)	108



Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

Net (decrease) increase in cash and cash equivalents	(11,212)	6,999
Cash and cash equivalents, beginning of period	63,359	31,179
Cash and cash equivalents, end of period	\$ 52,147	\$ 38,178
Supplemental disclosure of non-cash activities:		
Transfer of items originally classified as inventories to equipment	\$ 440	\$ 305
Issuance of equity for ODG contingent consideration (Note 5)	8,150	
Conversion of accounts receivable to investment in affiliate	332	

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

---

**Table of Contents**

**SEACHANGE INTERNATIONAL, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(unaudited)**

**1. Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements as of April 30, 2008 and for the three months ended April 30, 2008 and 2007 include the accounts of SeaChange International, Inc. and its subsidiaries ( SeaChange or the Company ). SeaChange believes that the unaudited condensed consolidated financial statements reflect all adjustments (consisting of only normal recurring adjustments), necessary for a fair statement of SeaChange s financial position, results of operations and cash flows at the dates and for the periods indicated. The results of operations for the periods presented are not necessarily indicative of results expected for the full fiscal year or any other future periods. The unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes for the year ended January 31, 2008, filed on April 14, 2008 included in SeaChange s Annual Report on Form 10-K for such fiscal year. The balance sheet at January 31, 2008 was derived from audited financial statements but does not include all disclosures required by accounting principles generally accepted in the United States of America.

**2. Significant Accounting Policies**

*Principles of Consolidation*

The Company consolidates the financial statements of its wholly owned subsidiaries and all inter-company accounts are eliminated in consolidation. SeaChange also holds minority investments in the capital stock of certain private companies having product offerings or customer relationships that have strategic importance. The Company evaluates its equity and debt investments and other contractual relationships with affiliate companies in order to determine whether the guidelines of FASB Interpretation ( FIN ) No. 46, Consolidation of Variable Interest Entities, as revised under FIN 46R should be applied in the financial statements. FIN No. 46R addresses consolidation by business enterprises of variable interest entities that possess certain characteristics. A variable interest entity ( VIE ) is defined as an entity in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. The primary beneficiary is required to consolidate the financial position and results of the VIE. Since the adoption of FIN 46R, the Company concluded that FIN 46R has not required the consolidation of any affiliated company.

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

**3. Fair Value Measurements**

The Company adopted the provisions of SFAS 157 and FSP FAS 157-2 on February 1, 2008. The adoption of these pronouncements did not have a material effect on the Company s financial position or results of operations. Accordingly, the Company is continuing to apply SFAS 115, *Accounting for Certain Investments in Debt and Equity Securities* (SFAS 115) for its available for sale securities with offsetting unrealized gains and losses reported in other comprehensive income or loss. Per SFAS 157, the Company is providing fair value measurement disclosures of its available for sale securities in accordance with one of three levels of fair value measurement.

SFAS 157 defines fair value to be the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and emphasizes that fair value is a market-based measurement, not an entity-specific measurement. It establishes a fair value hierarchy and expands disclosures about fair value measurements in both interim and annual periods. SFAS 157 enables the reader of the financial statements to assess the inputs used to develop fair value measurements by establishing a hierarchy for ranking the quality and reliability of the information used to determine fair values. FSP FAS 157-2 defers the effective date of SFAS 157 until January 2009 for non-financial assets and non-financial liabilities that are recognized or disclosed in the financial statements on a nonrecurring basis. SFAS 157 requires that assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

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



**Table of Contents**

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

The Company's financial assets and liabilities that are measured at fair value on a recurring basis as of April 30, 2008 are as follows:

	April 30, 2008	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
<b>Financial assets:</b>				
Available for sale marketable securities:				
Current marketable securities	\$ 20,065	\$ 20,065	\$	\$
Non-current marketable securities	6,749	6,749		
<b>Total</b>	<b>\$ 26,814</b>	<b>\$ 26,814</b>	<b>\$</b>	<b>\$</b>

The company relies on mark to market valuations to record the fair value of the Company's available for sale security assets and are measured under a Level 1 input. These assets are publicly traded equity securities for which market prices are readily observable and recorded under the guidelines of SFAS 115.

**4. Inventories**

Inventories consist of the following:

	Three months ended	
	April 30, 2008	January 31, 2008
(in thousands)		
Components and assemblies	\$ 11,932	\$ 9,979
Finished products	4,694	4,336
<b>Total inventory</b>	<b>\$ 16,626</b>	<b>\$ 14,315</b>

**5. Investments in Affiliates***On Demand Deutschland GmbH & Co. KG*

On February 27, 2007, the On Demand Group Ltd. ( ODG ), a wholly-owned U.K. subsidiary of SeaChange, entered into an agreement with Tele-Munchen Fernseh GmbH & Co. Produktionsgesellschaft (TMG) to create a joint venture named On Demand Deutschland GmbH & Co. KG. On Demand Deutschland specializes in establishing on-demand and pay-per-view services on multiple platforms in German-speaking Europe. ODG contributed \$2.8 million to acquire its 50% ownership interest in the joint venture of which \$2.6 million consisted of the fair value of customer contracts and content license agreements contributed by ODG and \$154,000 represented a cash contribution. The customer contracts and licensed content had no book value. SeaChange determined that this investment is an operating joint venture and does not require consolidation under the accounting guidance of FIN No. 46R. Consequently, SeaChange accounts for this investment under the equity method of accounting.

ODG's original investment in the joint venture was recorded at \$154,000 representing the US dollar equivalent of the initial cash contribution. The difference between the book and fair value of the customer contracts and content license agreements is being accreted over the expected five year life of the contracts and recorded as a gain and an increase in the investment. This gain will be partially offset by ODG's 50% share of the joint venture's amortization expense over the same period related to the acquired contracts and content license agreements. ODG also recorded a net payable amount to the joint venture of \$337,000 as of the joint venture formation date (February 27, 2007) reflecting the transfer of net

## Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

liabilities incurred by ODG related to the joint venture as well as the joint venture's reimbursement of previously incurred costs by ODG of \$787,000 related to joint venture activities prior to its formation. Consistent with EITF 89-7, *Exchange of Assets or Interest in a Subsidiary for a Noncontrolling Equity Interest in a New Entity*, ODG did not record other income in connection with the reimbursement of these costs or any other gains as ODG is deemed to have a commitment to support the operations of the joint venture. ODG treated the reimbursement and other gain for a total of \$869,000 as a capital distribution in excess of the

## Table of Contents

carrying value of its investment in the joint venture as of April 30, 2007. This capital distribution will be accreted over the expected five year life of the customer contracts and recorded as a gain and an increase in the investment in the joint venture. ODG recorded an income tax provision during the quarter ended April 30, 2007 of \$1.1 million for the taxable gain recognized by ODG related to the \$2.6 million contribution of customer contracts and content licenses to and the reimbursement of previously paid costs from the joint venture.

ODG entered into a Service Agreement with the joint venture whereby ODG provides content aggregation, distribution, marketing and administration services to the joint venture under an arm's length fee structure. In the three months ended April 30, 2008 and April 30, 2007, ODG recorded revenues of \$581,000 and \$233,000 (USD equivalent) respectively, related to the Service Agreement. ODG's share of profits from this agreement in proportion to its equity ownership interest is eliminated in consolidation.

The Shareholder's Agreement requires ODG to provide cash contributions up to \$4.2 million (USD equivalent) upon the request of the joint venture's management and approval by the shareholders of the joint venture. ODG recorded its proportionate share of the joint venture's losses for the three months ending April 30, 2008 and April 30, 2007 of \$283,000 and \$100,000 respectively. Due to the capital distribution and ODG's share of the joint venture's net loss exceeding the book value of its investment in the joint venture, the investment is recorded as a long-term liability of \$1.6 million and \$866,000 at April 30, 2008 and April 30, 2007, respectively.

### *InSite One*

In April 2008, the Company converted the outstanding accounts receivable balance of \$432,000 as of January 31, 2008 for \$100,000 and 474,300 shares of InSite One's Series E Convertible Preferred Stock owed to the Company by InSite One. The Company has approximately 12% share of the total capital stock of InSite One. SeaChange accounts for this investment under the cost method of accounting.

## **6. Commitments and Contingencies**

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

SeaChange enters into agreements in the ordinary course of business with customers, resellers, distributors, integrators and suppliers. Most of these agreements require SeaChange to defend and/or indemnify the other party against intellectual property infringement claims brought by a third party with respect to SeaChange's products. From time to time, SeaChange also indemnifies customers and business partners for damages, losses and liabilities they may suffer or incur relating to personal injury, personal property damage, product liability, and environmental claims relating to the use of SeaChange's products and services or resulting from the acts or omissions of SeaChange, its employees, authorized agents or subcontractors. For example, SeaChange has received requests from several of its customers for indemnification of patent litigation claims asserted by Acacia Media Technologies, USA Video Technology Corporation and VTran Media Technologies. Management performed an analysis of these requests under Statement of Financial Accounting Standards No. 5, *Accounting for Contingencies* (SFAS 5) and determined that, as of April 30, 2008, \$148,000 was estimable and probable and has recorded an accrual.

SeaChange warrants that its products, including software products, will substantially perform in accordance with its standard published specifications in effect at the time of delivery. Most warranties have at least a one year duration that generally commence upon installation. In addition, SeaChange provides maintenance support to all customers and therefore allocates a portion of the product purchase price to the initial warranty period and recognizes revenue on a straight line basis over that warranty period related to both the warranty obligation and the maintenance support agreement. When SeaChange receives revenue for extended warranties beyond the standard duration, it is deferred and recognized on a straight line basis over the contract period. Related costs are expensed as incurred.

In the ordinary course of business, SeaChange provides minimum purchase guarantees to certain of its vendors to ensure continuity of supply against the market demand. Although some of these guarantees provide penalties for cancellations and/or modifications to the purchase commitments as the market demand decreases, most of the guarantees do not. Therefore, as the market demand decreases, SeaChange re-evaluates the accounting implications of guarantees and determines what charges, if any, should be recorded.

## **Table of Contents**

With respect to its agreements covering product, business or entity divestitures and acquisitions, SeaChange provides certain representations and warranties and agrees to indemnify and hold such purchasers harmless against breaches of such representations, warranties and covenants. Many of the indemnification claims have a definite expiration date while some remain in force indefinitely. With respect to its acquisitions, SeaChange may, from time to time, assume the liability for certain events or occurrences that took place prior to the date of acquisition.

SeaChange provides such guarantees and indemnification obligations after considering the economics of the transaction and other factors including but not limited to the liquidity and credit risk of the other party in the transaction. SeaChange believes that the likelihood is remote that any such arrangement could have a material adverse effect on its financial position, results of operation or liquidity. SeaChange records liabilities, as disclosed above, for such guarantees based on the Company's best estimate of probable losses which considers amounts recoverable under any recourse provisions.

## **7. Segment Information**

Until the end of fiscal 2008, the Company was managed and operated as three segments, Broadcast, Broadband and Services. In its first quarter of fiscal 2009, the Company realigned its previously reported segments into three new reporting segments: Software, Servers and Storage, and Media Services, as segments as defined by SFAS No. 131, *Disclosure about Segments of an Enterprise and Related Information*. The Company believes this reorganization better reflects the increasing importance and magnitude of its software products and services as well as the scale of its subsidiary, The On Demand Group, Limited ( ODG ). A description of the three new reporting segments is as follows:

Software segment includes product revenues from the Company's Advertising, VOD, Middleware and Broadcast software, related services such as professional services, installation, training, project management, product maintenance, technical support and software development for those software products, and operating expenses relating to the Software segment such as research and development, selling and marketing and amortization of intangibles.

Servers and Storage segment includes product revenues from the VOD and Broadcast server product lines and related services such as professional services, installation, training, project management, product maintenance, and technical support for those products and operating expenses relating to the Servers and Storage segment, such as research and development and selling and marketing.

Media Services segment includes the operations of ODG including content acquisition, and preparation services for television service providers and related operating expenses.

Under this revised reporting structure, the Company further determined that there are significant functions, and therefore costs, that are considered corporate expenses and are not allocated to the reportable segments for the purposes of assessing performance and making operating decisions. These unallocated costs include general and administrative expenses, other than general and administrative expenses related to ODG, interest, taxes and equity earnings in affiliates, which are managed separately at the corporate level.

The segment data for the first quarter of fiscal 2008 has been recast to reflect the realignment of the new segments. Prior to fiscal 2009, services revenues, which included ODG revenues, were reported in the Services segment and the Company did not separately track these service revenues and costs by these new segments, except for ODG. Accordingly, management has made certain assumptions to determine the amount of service revenues and service costs attributed to the Software and Servers and Storage reporting segments for the first quarter of fiscal 2008. The basis of the assumptions for all such revenues, costs and expenses includes significant judgments and estimations. There are no inter-segment revenues for the periods shown below. The Company does not separately track all assets by operating segments nor are the segments evaluated under this criterion. The following summarizes the revenues, gross profit, operating expenses and income from operations by reportable segment:

**Table of Contents**

	Three months ended	
	April 30, 2008	April 30, 2007
<b>Software</b>		
Revenue:		
Products	\$ 19,153	\$ 15,337
Services	10,910	10,491
<b>Total revenue</b>	<b>30,063</b>	<b>25,828</b>
Gross profit	16,496	14,087
Operating expenses:		
Research and development	8,187	7,042
Selling and marketing	3,720	3,208
Amortization of intangibles	364	537
	12,271	10,787
<b>Income from operations</b>	<b>\$ 4,225</b>	<b>\$ 3,300</b>
<b>Servers and Storage</b>		
Revenue:		
Products	\$ 7,841	\$ 5,591
Services	3,466	3,042
<b>Total revenue</b>	<b>11,307</b>	<b>8,633</b>
Gross profit	5,599	3,096
Operating expenses:		
Research and development	2,289	3,295
Selling and marketing	2,673	2,516
	4,962	5,811
<b>Income (loss) from operations</b>	<b>\$ 637</b>	<b>\$ (2,715)</b>
<b>Media Services</b>		
Service revenue	\$ 4,014	\$ 4,383
Gross profit	667	634
Operating expenses:		
Selling and marketing	30	61
General and administrative	815	585
Amortization of intangibles	32	260
	877	906
<b>Loss from operations</b>	<b>\$ (210)</b>	<b>\$ (272)</b>
<b>Unallocated Corporate</b>		
Operating expenses:		
General and administrative	\$ 4,296	\$ 4,318
<b>Total unallocated corporate expenses</b>	<b>\$ 4,296</b>	<b>\$ 4,318</b>
<b>Consolidated income (loss) from operations</b>	<b>\$ 356</b>	<b>\$ (4,005)</b>





**Table of Contents**

The following table summarizes revenues by geographic locations:

	<b>Three months ended</b>	
	<b>April 30,</b>	<b>April 30,</b>
	<b>2008</b>	<b>2007</b>
	<b>(in thousands)</b>	
<b>Revenues:</b>		
United States of America	\$ 31,484	\$ 24,816
United Kingdom	7,727	7,391
Canada and South America	957	2,660
Europe and Middle East (excluding the United Kingdom)	1,860	2,101
Asia Pacific and other international locations	3,356	1,876
<b>Total</b>	<b>\$ 45,384</b>	<b>\$ 38,844</b>

The following summarizes revenues by significant customer where such revenue exceeded 10% of total revenues for the indicated period:

	<b>Three months ended</b>	
	<b>April 30,</b>	<b>April 30,</b>
	<b>2008</b>	<b>2007</b>
	<b>(in thousands)</b>	
Customer A	27%	33%
Customer B	13%	16%

International sales accounted for approximately 31% and 36% of total revenues in the three-month periods ended April 30, 2008 and 2007, respectively. For the three months ended April 30, 2008 and 2007, the Company's sales were made primarily in United States dollars. Therefore, SeaChange has not experienced any material impact from fluctuations in foreign currency exchange rates on its results of operations or financial position.

At April 30, 2008, two different customers accounted for approximately 30% and 15%, respectively, of the accounts receivable and unbilled receivables balances, and at January 31, 2008, two customers accounted for 23% and 18%, respectively, of SeaChange's accounts receivable and unbilled receivables balances.

Goodwill allocated to the Company's new reportable segments and changes in the carrying amount of goodwill for the first three months of fiscal 2009 were as follows:

	<b>Goodwill</b>					
	<b>Broadband</b>	<b>Services</b>	<b>Software</b>	<b>Servers &amp; Storage</b>	<b>Media Services</b>	<b>Total</b>
	<b>(in thousands)</b>					
Balance at January 31, 2008	\$ 11,169	\$ 18,302	\$	\$	\$	\$ 29,471
Reallocation	(11,169)	(18,302)	10,611	558	18,302	
Cumulative Translation Adjustment					(73)	(73)
Balance at April 30, 2008	\$	\$	\$ 10,611	\$ 558	\$ 18,229	\$ 29,398

The goodwill reallocation shown in the table above relates to the reorganization of the Company's reportable segments. The goodwill formerly included in the Broadband and Services segments was allocated between the Software, Servers and Storage and Media Services segments based on a relative fair value approach using management estimates of fair value of the segments. No impairment was recorded as a result of the change in segments.

**8. Income Taxes**

For the three months ended April 30, 2008, the Company recorded an income tax provision of \$425,000 on a profit before tax of \$1.1 million, resulting in an effective income tax provision rate of 40.4%. For the three months ended April 30, 2007, the Company recorded an income tax provision of \$1.3 million on a loss before tax of \$3.5 million, resulting in an effective income tax provision rate of (35.7%). Of this amount, \$1.1 million was attributable to taxable gains for ODG's transfer of assets to and the reimbursement of previously paid costs from On Demand Deutschland GmbH & Co. KG, the German joint

**Table of Contents**

venture formed in February 2007 with Tele-Munchen Fernseh GmbH & Co. Produktionsgesellschaft. In addition, the Company exhausted its U.S. tax benefit carry back potential in fiscal 2007, thus eliminating any recording of U.S. tax benefit for fiscal 2008.

As of April 30, 2008, the Company has maintained the full valuation allowance against its net U.S. deferred tax assets primarily due to the uncertainties related to the Company's ability to generate sufficient pre-tax income for fiscal 2009 and thereafter. If SeaChange generates sufficient pre-tax income in the future, some portion or all of the valuation allowance could be reversed and a corresponding increase in net income would be reported in future periods.

**9. Comprehensive Income (Loss)**

The components of comprehensive income (loss) consisted of the following:

	<b>Three months ended</b>	
	<b>April 30,</b>	<b>April 30,</b>
	<b>2008</b>	<b>2007</b>
	<b>(in thousands)</b>	
Net income (loss)	\$ 343	\$ (4,583)
Other comprehensive income (loss):		
Foreign currency translation adjustment	(176)	389
Unrealized gain on marketable securities	(114)	26
Other comprehensive (loss) income	(290)	415
Comprehensive income (loss)	\$ 53	\$ (4,168)

**10. Earnings (Loss) Per Share**

Earnings (loss) per share are presented in accordance with SFAS No. 128, Earnings Per Share, which requires the presentation of basic earnings (loss) per share and diluted earnings (loss) per share. Basic earnings (loss) per share is computed by dividing earnings (loss) available to common shareholders by the weighted-average shares of common stock outstanding during the period. For the purposes of calculating diluted earnings (loss) per share, the denominator includes both the weighted average number of shares of common stock outstanding during the period and the weighted average number of shares of potential common stock, such as stock options and restricted stock units and warrants, calculated using the treasury stock method.

4,565,799 stock options outstanding for the three months ended April 30, 2008 were anti-dilutive based on the Company's stock price being lower than the option exercise price. The number of options that were anti-dilutive at April 30, 2007 as a result of the Company's net losses were 4,262,365 shares. The dilutive effect was not included in the calculation for April 30, 2007 as a result.

Below is a summary of the shares used in calculating basic and diluted income (loss) per share for the periods indicated:

	<b>Three months ended</b>	
	<b>April 30,</b>	<b>April 30,</b>
	<b>2008</b>	<b>2007</b>
	<b>(in thousands)</b>	
Weighted average shares used in calculating earnings per share - Basic	30,477	29,389
Dilutive common stock options	340	
Weighted average shares used in calculating earnings per share - Diluted	30,817	29,389

**11. Subsequent Events**

## Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

On June 3, 2008 ODG executed an agreement to purchase a 9,000 square foot facility in London, UK for approximately GBP 2.7 million (\$5.4 million equivalent). This facility will be used as office space for ODG personnel as well as housing content preparation activities. The closing is expected by the end of June. The Company plans to fund the purchase of this facility, together with the purchase of production and office equipment of approximately GBP 2.0 million (\$4.0 million equivalent) with available cash.

**Table of Contents****12. Recently Issued Accounting Pronouncements**

In December 2007, Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 141(R) *Business Combinations* ( SFAS 141R ). SFAS 141R establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree. SFAS 141R also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The guidance will become effective for fiscal years beginning after December 15, 2008. SFAS No. 141R is effective for the Company beginning February 1, 2009.

In December 2007, the FASB issued SFAS No. 160 *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51* ( SFAS 160 ). SFAS 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. The guidance will become effective for fiscal years beginning after December 15, 2008. SFAS 160 is effective for the Company beginning February 1, 2009. The Company is currently assessing the impact that FASB 160 may have on its results of operations and financial position.

In March 2008, the FASB issued FASB Statement No. 161 ( SFAS 161 ), *Disclosures about Derivative Instruments and Hedging Activities*. SFAS 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows. It is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. The Company is currently evaluating the impact of adopting SFAS 161 on its results of operations and financial position.

On May 9, 2008, the FASB issued FASB Statement No. 162, *The Hierarchy of Generally Accepted Accounting Principles* ( SFAS 162 ). The new standard is intended to improve financial reporting by identifying a consistent framework, or hierarchy, for selecting accounting principles to be used in preparing financial statements that are presented in conformity with U.S. generally accepted accounting principles ( GAAP ) for nongovernmental entities. Prior to the issuance of SFAS 162, GAAP hierarchy was defined for public accountants and their firms in the American Institute of Certified Public Accountants (AICPA) Statement on Auditing Standards (SAS) No. 69, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles* . SFAS 162 states that the GAAP hierarchy should be directed to entities because it is the entity (not its auditor) that is responsible for selecting accounting principles for financial statements that are presented in conformity with GAAP. SFAS 162 is effective 60 days following the Security Exchange Commission's approval of the Public Company Accounting Oversight Board Auditing amendments to AU Section 411, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles* . The adoption of SFAS 162 is not expected to have a material impact on the Company's position.

On December 12, 2007, the FASB ratified Emerging Issues Task Force ( EITF ) Issue No. 07-01, *Accounting for Collaborative Arrangements* ( EITF 07-01 ). EITF 07-01 defines collaborative arrangements and establishes reporting requirements for transactions between participants in a collaborative arrangement and between participants in the arrangement and third parties. EITF 07-01 also establishes the appropriate income statement presentation and classification for joint operating activities and payments between participants, as well as the sufficiency of the disclosures related to these arrangements. EITF 07-01 is effective for fiscal years beginning after December 15, 2008 (February 1, 2009, for the Company). Companies are required to apply EITF 07-01 using a modified version of retrospective transition for those arrangements in place at the effective date. In addition, companies are required to report the effects of the application of EITF 07-01 as a change in accounting principle through retrospective application to all prior periods presented for all arrangements existing as of the effective date, unless it is impracticable to apply the effects of the change retrospectively. The Company is currently assessing the impact that EITF 07-01 may have on its results of operations and financial position.

On April 25, 2008, the FASB issued FASB Staff Position ( FSP ) FAS 142-3, *Determination of the Useful Life of Intangible Assets*, which revises the factors that an entity should consider to develop renewal or extension assumptions used in determining the useful life of a recognized intangible asset. The FSP amends paragraph 11(d) of FAS 142. The FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008 (February 1, 2009, for the Company) and for interim periods within those fiscal years. Early adoption is prohibited. Entities should apply the FSP's guidance on determining the useful life of an intangible asset prospectively to recognized intangible assets acquired after the

**Table of Contents**

FSP's effective date. However, once effective, the FSP's disclosure requirements apply prospectively to all recognized intangible assets, including those acquired before the FSP's effective date. The Company is currently assessing the impact that FAS 142-3 may have on its results of operations and financial position.

***Impact of the Recently Adopted Accounting Pronouncements***

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurement* ( SFAS 157 ). SFAS 157 defines fair value, establishes a framework for measuring fair value using generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement does not require any new fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. Effective February 1, 2008 the Company has made additional disclosures upon the adoption of SFAS 157 regarding fair valuation of its investments for our available-for-sale marketable securities. The impact of this adoption did not materially affect the Company's results of operations and financial position.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ( SFAS 159 ). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The impact of this adoption did not materially affect the Company's results of operations and financial position.

**ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
***Factors That May Affect Future Results***

Any statements contained in this Form 10-Q that do not describe historical facts may constitute forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. These statements relate to future events or our future financial performance and are identified by words such as may, will, could, should, expect, plan, intend, seek, anticipate, believe, estimate, comparable terms or the negative of those terms. Forward-looking statements in this Form 10-Q include certain statements regarding the effect of certain accounting standards on our financial position and results of operations, the effect of certain legal claims against us, projected changes in our revenues, earnings and expenses, exchange rate sensitivity, interest rate sensitivity, liquidity, product introductions and general market conditions. Our actual future results may differ significantly from those stated in any forward-looking statements. Any such forward-looking statements contained herein are based on current expectations, but are subject to a number of risks and uncertainties that may cause actual results to differ materially from expectations. The factors that could cause actual future results to differ materially from current expectations include the following: the continued growth, development and acceptance of the video-on-demand market; the loss of one of our large customers; the cancellation or deferral of purchases of our products; the timing of significant customer orders; the length of our sales cycles; a decline in demand or average selling price for our broadband products; our ability to manage our growth; our ability to integrate businesses acquired by us; our ability to protect our intellectual property rights and the expenses that may be incurred by us to protect our intellectual property rights; an unfavorable result of current or future litigation; content providers limiting the scope of content licensed for use in the video-on-demand market; our ability to introduce new products or enhancements to existing products; our dependence on certain sole source suppliers and third-party manufacturers; our ability to obtain license or distribution rights for certain technologies; our ability to compete in our marketplace; our ability to respond to changing technologies; the risks associated with international sales; the performance of companies in which we have made equity investments, including Casa Systems, Inc., and On Demand Deutschland GmbH & Co. KG; changes in the regulatory environment and our ability to hire and retain highly skilled employees; our current ineligibility to use a registration statement on Form-S3; any weaknesses over internal controls over financial reporting; any additional tax liabilities; system errors, failures or interruptions. Further information on factors, including those listed above, that could cause actual results to differ from those anticipated is detailed in various filings made by us from time to time with the Securities and Exchange Commission, including but not limited to, those appearing in Part I, Item 1A. Risk Factors, in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on April 14, 2008. Any forward looking statements should be considered in light of those factors.

***Overview***

We are a leading developer, manufacturer and marketer of digital video systems and services including the management, aggregation, licensing, storage, and distribution of video, television, gaming and advertisement content to cable system operators, telecommunications companies and broadcast television companies.





## Table of Contents

Until the end of fiscal 2008, the Company was managed and operated as three segments, Broadcast, Broadband and Services. In its first quarter of fiscal 2009, the Company realigned its previously reported segments into three new reporting segments: Software, Servers and Storage, and Media Services as segments as defined by SFAS No. 131, *Disclosure about Segments of an Enterprise and Related Information*. The Company believes this reorganization better reflects the increasing importance and magnitude of its software products and services as well as the scale of its subsidiary, The On Demand Group Limited ( ODG ). A description of the three new reporting segments is as follows:

Software segment includes product revenues from the Company's Advertising, VOD, Middleware and Broadcast software, related services such as professional services, installation, training, project management, product maintenance, technical support and software development for those software products, and operating expenses relating to the Software segment such as research and development, selling and marketing and amortization of intangibles.

Servers and Storage segment includes product revenues from VOD and Broadcast server product lines and related services such as professional services, installation, training, project management, product maintenance, and technical support for those products and operating expenses relating to the Servers and Storage segment, such as research and development and selling and marketing.

Media Services segment includes the operations of ODG including content acquisition, and preparation services for television service providers and related operating expenses.

Under this revised reporting structure, the Company determined there are significant functions, and therefore costs, that are considered corporate expenses and are not allocated to the reportable segments for the purposes of assessing performance and making operating decisions. These unallocated costs include general and administrative expenses, other than general and administrative expenses related to ODG, interest, taxes and equity earnings in affiliates, which are managed separately at the corporate level.

The Segment data for the first quarter of fiscal 2008 has been recast to reflect the realignment of the new segments. Prior to fiscal 2009, services revenues, which included ODG revenues, were reported in the Services segment and the Company did not separately track these service revenues and costs by these new segments, except for ODG. Accordingly, management has made certain assumptions to determine the amount of service revenues and service costs attributed to the Software and Servers and Storage reporting segments for the first quarter of fiscal 2008. The basis of the assumptions for all such revenues, costs and expenses includes significant judgments and estimations. There are no inter-segment revenues for the periods shown below. The Company does not separately track all assets by operating segments nor are the segments evaluated under this criterion.

We have experienced fluctuations in our product revenues from quarter to quarter due to the timing of the receipt of customer orders and the shipment of those orders. The factors that impact the timing of the receipt of customer orders include among other factors:

the customer's receipt of authorized signatures on their purchase orders;

the budgetary approvals within the customer's company for capital purchases; and

the ability to process the purchase order within the customer's organization in a timely manner.

Factors that may impact the shipment of customer orders include:

the availability of material to produce the product;

the time required to produce and test the product before delivery; and

the customer's required delivery date.

The delay in the timing of receipt and shipment of any one customer order can result in significant fluctuations in our revenue reported on a quarterly basis.

Our operating results are significantly influenced by a number of factors, including the mix of products sold and services provided, pricing, costs of materials used in our products and the expansion of our operations during the fiscal year. We price our products and services based upon our costs and consideration of the prices of competitive products and services in the marketplace. The costs of our products primarily consist of the costs of components and subassemblies that have generally declined from product introduction to product maturity. As a result of the growth of our business, our operating expenses have historically increased in the areas of research and development, selling and marketing and administration. In the current state of the economy, we currently expect that customers may still have limited capital spending budgets as we believe they

**Table of Contents**

are dependent on advertising revenues to fund their capital equipment purchases. Accordingly, we expect our financial results to vary from quarter to quarter and our historical financial results are not necessarily indicative of future performance. In light of the higher proportion of our international business, we expect movements in foreign exchange rates to have a greater impact on our operating results and the equity section of our balance sheet in the future.

Our ability to continue to generate revenues within the markets that our products are sold and to generate cash from operations and net income is dependent on several factors which include:

market acceptance of the products and services offered by our customers and increased subscriber usage and demand for these products and services;

selection by our customers of our products and services versus the products and services being offered by our competitors;

our ability to introduce new products to the market in a timely manner and to meet the demands of the market for new products and product enhancements;

our ability to maintain gross margins from the sale of our products and services at a level that will provide us with cash to fund our operations given the pricing pressures within the market and the costs of materials to manufacture our products; and

our ability to control operating costs given the fluctuations that we have experienced with revenues from quarter to quarter.

**Results of Operations**

The following table sets forth statement of operations data for the three months ended April 30, 2008 compared to the three months ended April 30, 2007.

	<b>Three Months Ended</b>	
	<b>April 30, 2008</b>	<b>April 30, 2007</b>
	<b>(in thousand)</b>	
<b>Revenues:</b>		
Products	\$ 26,994	\$ 20,928
Services	18,390	17,916
	45,384	38,844
<b>Costs and expenses:</b>		
Cost of product revenues	10,725	9,362
Cost of service revenues	11,897	11,665
Research and development	10,476	10,337
Selling and marketing	6,423	5,785
General and administrative	5,111	4,903
Amortization of intangibles	396	797
Income (loss) from operations	356	(4,005)
Interest and other income, net	695	467
Income (loss) before income taxes and equity income in earnings of affiliates	1,051	(3,538)
Income tax expense	(425)	(1,263)

## Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

Equity (loss) income in earnings of affiliates, net of tax	(283)	218
Net income (loss)	\$ 343	\$ (4,583)

### ***Revenues***

The following table summarizes information about the Company's reportable segment revenues for the three months ended April 30, 2008 and 2007. Segment data for April 30, 2007 is also presented on a basis consistent with the April 30, 2008 data and the changed reporting segment structure.

**Table of Contents**

	Three months ended		Increase (Decrease)	
	April 30, 2008	April 30, 2007	\$	%
<b>(in thousands, except for percentage data)</b>				
<b>Software revenues:</b>				
Product	\$ 19,153	\$ 15,337	\$ 3,816	25%
Services	10,910	10,491	419	4%
Total Software revenues	\$ 30,063	\$ 25,828	\$ 4,235	16%
<b>Servers and Storage revenues:</b>				
Product	\$ 7,841	\$ 5,591	\$ 2,250	40%
Services	3,466	3,042	424	14%
Total Servers and Storage revenues	\$ 11,307	\$ 8,633	\$ 2,674	31%
<b>Media Services:</b>				
Services	\$ 4,014	\$ 4,383	\$ (369)	-8%
<b>Total consolidated revenue:</b>				
Product	\$ 26,994	\$ 20,928	\$ 6,066	29%
Services	18,390	17,916	474	3%
Total consolidated revenues	\$ 45,384	\$ 38,844	\$ 6,540	17%

*Product Revenues.* Product revenues increased 29% to \$27.0 million in the three months ended April 30, 2008 from \$20.9 million in the three months ended April 30, 2007. Product revenues from the Software segment accounted for 71% and 73% of the total product revenue and the Servers and Storage segment, accounted for 29% and 27% of total product revenues in the three months ended April 30, 2008 and April 30, 2007, respectively.

*Services Revenues.* Our Services revenues increased 3% year over year to \$18.4 million in the three months ended April 30, 2008 from \$17.9 million in the three months ended April 30, 2007. Service revenues for the Software segment accounted for 59% of the total Services revenue in three months ended April 30, 2008 and April 30, 2007. Servers and Storage service revenue accounted for 19% and 17% of total services revenues in three months ended April 30, 2008 and April 30, 2007, respectively, while Media Services revenue accounted for 22% and 24% of total services revenues in three months ended April 30, 2008 and April 30, 2007, respectively. We expect revenues from services to continue to grow year-over-year from our expanding installed base of products and additional service offerings.

For the three months ended April 30, 2008 two customers accounted for more than 40% of our total revenues, and the same two customers accounted for more than 49% of our total revenues for the three months ended April 30, 2007. Revenue from each of these customers was comprised of Software and Servers and Storage segment revenues. We believe that a significant amount of our revenues will continue to be derived from a limited number of customers.

International sales accounted for approximately 31% and 36% of total revenues in the three months ended April 30, 2008 and April 30, 2007, respectively. The U.S. and the United Kingdom together accounted for 86% and 83% of total revenue for the three months ended April 30, 2008 and 2007, respectively. These orders were made primarily in United States dollars. We expect that international products and services revenues will remain a significant portion of our business in the future.

*Software Revenues.* Revenues from our Software segment for the three months ended April 30, 2008 increased \$4.2 million, or a 16% increase from the three months ended April 30, 2007. The year over year growth was primarily due to increased software licensing revenue from shipments of Axiom, VODlink and our VOD hospitality software products which was partially offset by lower software revenues from Comcast. The 4% increase in services revenue for the Software segment was primarily due to VOD product maintenance contracts and other technical support services from a growing installed base of products.

*Servers and Storage Revenues.* Revenues from the Servers and Storage segment for the three months ended April 30, 2008 increased \$2.7 million or 31% from related revenues in the three months ended April 30, 2007. The increase of product revenues in the three months ended April 30, 2008 of \$2.2 million compared to the same quarter in the previous year was primarily due to higher Broadcast server revenue from Europe and Asia as well as \$1.6 million of lower deferred revenue



## **Table of Contents**

from Comcast tied to a higher level of contract undeliverables in the first quarter of fiscal 2008 compared to the first quarter of fiscal 2009. The 14% year over year increase in services revenue in our Servers and Storage segment is due to a larger installed base of our VOD and broadcast servers products.

*Media Services.* Revenues from Media Services decreased by approximately \$400,000 or 8% in the three months ended April 30, 2008 compared to the three months ended April 30, 2007. The decrease in revenue was due primarily to lower ODG professional services from Latin American customers in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008.

*Product Gross Profit.* Costs of product revenues consist primarily of the cost of purchased material components and subassemblies, labor and overhead relating to the final assembly and testing of complete systems and related expenses. The gross profit percentage for products increased from 55% in the three months ended April 30, 2007 to 60% in three months ended April 30, 2008. The increase in product gross profit percentages between years is due mainly to a favorable product mix of higher margin software products in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008 along with lower manufacturing costs due to headcount and other cost reductions taken in the second fiscal quarter of last year.

*Services Gross Profit.* Cost of services revenues consist primarily of labor, materials and overhead relating to the installation, training, product maintenance and technical support, software development, and project management provided by us and costs associated with providing video content services. The gross profit percentage for services was flat at 35% compared to last year. We expect that Services gross profit will increase in the future due to the growing installed base of systems, but may be impacted by the timing of costs associated with our ongoing investment required to expand our service organization in order to support our installed base of products.

*Software Revenues Gross Profit.* Software segment gross margin was 55% in the three months ended April 30, 2008 and April 30, 2007.

*Servers and Storage Gross Profit.* Servers and Storage segment gross margin of 50% in the three months ended April 30, 2008 was fourteen points higher than in the three months ended April 30, 2007 due mainly to higher VOD and Broadcast server margins, resulting from improvements in manufacturing costs, favorable pricing and lower service personnel costs.

*Media Services Gross Profit.* Media Services segment gross margin of 17% in the three months ended April 30, 2008 was two points higher than in the three months ended April 30, 2007 due principally to a greater proportion of higher margin content aggregation services in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008.

*Research and Development.* Research and development expenses consist primarily of the compensation of development personnel, depreciation of development and test equipment and an allocation of related facilities expenses. Research and development expenses increased 1% from \$10.3 million or 27% of total revenues, in the three months ended April 30, 2007, to \$10.5 million or 23% of total revenues, in the three months ended April 30, 2008. The increase is primarily due to lower absorption of research and development expenses resulting from a decrease in software development revenue for the three months ended April 30, 2008, compared to the three months ended April 30, 2007. We expect that research and development will continue to increase in fiscal year 2009 as we continue development of new products and enhancements to existing products.

*Selling and Marketing.* Selling and marketing expenses consist primarily of compensation expenses, including sales commissions, travel expenses and certain promotional expenses. Selling and marketing expenses increased 11% from \$5.8 million or 15% of total revenues, in the three months ended April 30, 2007, to \$6.4 million, or 14% of total revenues, in the three months ended April 30, 2008. This increase is primarily due to increased staffing, and \$300,000 of higher commission expense related to higher revenues.

*General and Administrative.* General and administrative expenses consist primarily of the compensation of executive, finance, human resource and administrative personnel, legal and accounting services and an allocation of related facilities expenses. In the three months ended April 30, 2008, general and administrative expenses increased to \$5.1 million, or 11% of total revenues, from \$4.9 million, or 13% of total revenues, in the three months ended April 30, 2007. The increase was primarily due to increased headcount related expenses at ODG compared to the same period in the prior fiscal year.

*Amortization of intangible assets.* Amortization expense consists of the amortization of acquired intangible assets which are operating expenses and not considered costs of revenues. Amortization expense was \$396,000 in the three months ended April 30, 2008 and \$797,000 in the three months ended April 30, 2007. The sale of the Company's equity investment in FilmFlex and the removal of the intangible assets related to FilmFlex contributed to the decrease in amortization expense.





**Table of Contents**

Amortization is also based on the future economic value of the related intangible assets which is generally higher in earlier years of the assets lives. An additional \$92,000 and \$121,000 of amortization expense related to acquired technology was charged to cost of sales for the three months ended April 30, 2008 and 2007, respectively.

*Interest and Other Income.* Interest income was \$695,000 in the three months ended April 30, 2008, compared to \$468,000 in the three months ended April 30, 2007. The increase in interest income is primarily due to an increase in the cash position of the Company compared to April 30, 2007 due mainly to \$18 million of proceeds received in the fourth quarter of fiscal 2008 related to the sale of our equity investment in Filmflex.

*Equity (Loss) Income in Earnings of Affiliates.* Equity loss in earnings of affiliates was \$283,000 in the three months ended April 30, 2008 in comparison to equity income in earnings of affiliates of \$218,000 in the three months ended April 30, 2007. For the three months ended April 30, 2008, \$283,000 of equity loss was recognized from On Demand Deutschland. The On Demand Deutschland loss was net of \$179,000 in accreted gains related to the customer contracts and content licensing agreements and the capital distribution related to reimbursement of previously incurred costs. For the three months ended April 30, 2007, \$318,000 of equity income was recognized from FilmFlex and \$100,000 of equity loss was recognized from On Demand Deutschland. The On Demand Deutschland loss was net of \$120,000 in accreted gains related to the customer contracts and content licensing agreements and the capital distribution related to reimbursement of previously incurred costs.

*Income Tax Provision and Benefit.* For the three months ended April 30, 2008, we recorded an income tax provision of \$425,000 on income before tax of \$1.1 million resulting in an effective income tax provision rate of 40.4%. The income tax provision was primarily attributable to the taxable position of our foreign subsidiaries. In addition, we have exhausted our U.S. tax benefit carry back thus eliminating any recording of U.S. tax benefit for fiscal 2009. As of April 30, 2008, we continue to maintain a full valuation allowance against our net U.S. deferred tax assets primarily due to the uncertainties related to our ability to generate sufficient pre-tax income for fiscal 2009 and thereafter. If we generate sufficient pre-tax income in the future, some portion or all of the valuation allowance could be reversed and a corresponding increase in net income would be reported in future periods.

***Off-Balance Sheet Arrangements***

We do not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements. As such, we are not exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

***Liquidity and Capital Resources***

Historically, we have financed our operations and capital expenditures primarily with cash on-hand and the proceeds from sales of our common stock. Cash and cash equivalents decreased \$11.3 million from \$63.4 million at January 31, 2008 to \$52.1 million at April 30, 2008. Working capital, excluding long-term marketable securities, increased from \$86.2 million at January 31, 2008 to \$93.1 million at April 30, 2008.

Net cash used by operating activities was \$7.3 million for the three months ended April 30, 2008 compared to net cash provided by operating activities of \$2.0 million for the three months ended April 30, 2007. The net cash used by operating activities for the three months ended April 30, 2008 was the result of an increase in net receivables of \$13 million and an increase in inventories of \$3 million offset by non cash expenses of \$3.9 million and an increase in deferred revenue of \$5.6 million. The increases in net receivables, inventories and deferred revenues were due to the timing of shipments and invoicing to our customers during the quarter. It is typical for us to experience fluctuations in our operating results primarily due to the timing of receiving customer orders and the related shipment of these customer orders. As a result of these monthly fluctuations, we may experience significant:

increases or decreases in our inventories as a result of the timing of the procurement of components for anticipated orders for our product segments;

increases or decreases in our accounts payable balance primarily due to the timing of payments for materials purchased for prior month shipments; and

## Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

increases or decreases in our accounts receivable balances and customer deposits as a result of the timing of receiving customer orders during the period and of customer payments.

Net cash used by investing activities was \$2.3 million for the three months ended April 30, 2008 compared to net cash provided by investing activities of \$4.8 million for the three months ended April 30, 2007. Investment activity for the three months ended April 30, 2008 consisted primarily of the net purchase of \$1.4 million of marketable securities, and the purchase of property and equipment of \$715,000.

---

## **Table of Contents**

Net cash used by financing activities was \$1.5 million for the three months ended April 30, 2008 and net cash provided by financing activities was \$136,000 for the three months ended April 30, 2007. In the three months ended April 30, 2008, the cash used by financing activities was due to the repurchase of \$1.8 million of the Company's stock partially offset by the proceeds from the issuance of common stock in connection with stock option exercises of \$330,000 and the vesting of restricted stock units.

We maintain a \$15.0 million revolving line of credit with Citizens Bank (a subsidiary of the Royal Bank of Scotland Group plc). Loans made under this revolving line of credit bear interest at a rate per annum equal to the bank's prime rate. Borrowings under this line of credit are collateralized by substantially all of our assets. The loan agreement requires that we provide Citizens Bank with certain periodic financial reports and comply with certain financial ratios including a minimum level of earnings before interest, taxes and depreciation and amortization on a trailing twelve month basis, when amounts are outstanding under the loan agreement. As of April 30, 2008, we were in compliance with the financial covenants. There are currently no amounts outstanding under the revolving line of credit.

On February 27, 2007, the On Demand Group Ltd. ( ODG ), a wholly-owned U.K. subsidiary of SeaChange, entered into an agreement with Tele-Munchen Fernseh GmbH & Co. Produktionsgesellschaft (TMG) to create a joint venture named On Demand Deutschland GmbH & Co. KG. The Shareholder's Agreement requires ODG to provide cash contributions up to \$4.2 million (USD equivalent) upon the request of the joint venture's management and approval by the shareholders of the joint venture.

On February 13, 2008, SeaChange International's Board of Directors authorized the repurchase of up to \$20.0 million of its common stock, par value \$.01 per share, through a share repurchase program. As authorized by the program, shares may be purchased in the open market or through privately negotiated transactions, in a manner consistent with applicable securities laws and regulations, including pursuant to Rule 10b5-1 plan maintained by the Company. This stock repurchase program does not obligate the Company to acquire any specific number of shares and may be suspended or discontinued at any time. All repurchases are expected to be funded from the Company's current cash and investments balances. The timing and amount of the shares to be repurchased will be based on market conditions and other factors, including price, corporate and regulatory requirements and alternative investment opportunities. As of April 30, 2008, 282,675 shares of our common stock had been purchased as part of the repurchase program at an average price of \$7.01, all of which was purchased during the three months ended April 30, 2008 at an average price of \$7.01. As of April 30, 2008 the remaining maximum dollar value of shares that may yet be purchased under the program is \$18.0 million.

On June 3, 2008, ODG executed an agreement to purchase a 9,000 square foot facility in London, UK for approximately GBP 2.7 million (\$5.4 million equivalent). This facility will be used as office space for ODG personnel as well as housing content preparation activities, and preparation work. The closing is expected by the end of June. The Company plans to fund the purchase of this facility, together with the purchase of production and office equipment of approximately GBP 2.0 million (\$4.0 million equivalent) with available cash.

We believe that existing funds combined with available borrowings under the revolving line of credit and cash provided by future operating activities are adequate to satisfy our working capital, potential acquisitions and capital expenditure requirements and other contractual obligations for the foreseeable future, including at least the next 24 months.

### ***Effects of Inflation***

Management believes that financial results have not been significantly impacted by inflation and price changes in materials we use in manufacturing our products.

### ***Significant Accounting Policies***

#### ***Principles of Consolidation***

The Company consolidates the financial statements of its wholly owned subsidiaries and all inter-company accounts are eliminated in consolidation. SeaChange also holds minority investments in the capital stock of certain private companies having product offerings or customer relationships that have strategic importance. The Company evaluates its equity and debt investments and other contractual relationships with affiliate companies in order to determine whether the guidelines of FASB Interpretation ( FIN ) No. 46, Consolidation of Variable Interest Entities, as revised under FIN 46R should be applied in the financial statements. FIN No. 46R addresses consolidation by business enterprises of variable interest entities

---

**Table of Contents**

that possess certain characteristics. A variable interest entity ( VIE ) is defined as an entity in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. The primary beneficiary is required to consolidate the financial position and results of the VIE. Since the adoption of FIN 46R, the Company concluded that FIN 46R has not required the consolidation of any affiliated company.

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

*Revenue Recognition and Allowance for Doubtful Accounts*

Revenues from sales of hardware, software and systems that do not require significant modification or customization of the underlying software are recognized when title and risk of loss has passed to the customer, there is evidence of an arrangement, fees are fixed or determinable and collection of the related receivable is considered probable. Customers are billed for installation, training, project management and at least one year of product maintenance and technical support at the time of the product sale. Revenue from these activities are deferred at the time of the product sale and recognized ratably over the period these services are performed. Revenue from ongoing product maintenance and technical support agreements are recognized ratably over the period of the related agreements. Revenue from software development contracts that include significant modification or customization, including software product enhancements, is recognized based on the percentage of completion contract accounting method using labor efforts expended in relation to estimates of total labor efforts to complete the contract. For contracts, where some level of profit is assured but the Company is only able to estimate ranges of amounts of total contract revenue and total contract cost, SeaChange uses the lowest probable level of profits in accounting for the contract revenues and costs. Accounting for contract amendments and customer change orders are included in contract accounting when executed. Revenue from shipping and handling costs and other out-of-pocket expenses reimbursed by customers are included in revenues and cost of revenues. SeaChange's share of intercompany profits associated with sales and services provided to affiliated companies are eliminated in consolidation in proportion to our equity ownership.

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

SeaChange recognizes revenue for product and services only in those situations where collection from the customer is probable. The Company performs ongoing credit evaluations of customers' financial condition but generally does not require collateral. For some international customers, SeaChange requires an irrevocable letter of credit to be issued by the customer before the purchase order is accepted. The Company monitors payments from customers and assesses any collection issues. The Company maintains allowances for specific doubtful accounts and other risk categories of accounts based on estimates of losses resulting from the inability of the Company's customers to make required payments and records these allowances as a charge to general and administrative expenses. SeaChange bases its allowances for doubtful accounts on historical collections and write-off experience, current trends, credit assessments, and other analysis of specific customer situations.

Any taxes assessed by a governmental authority related to revenue-producing transactions (e.g. sales or value-added taxes) are reported on a net basis and excluded from revenues.

**Table of Contents***Use of Estimates*

The preparation of these financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosure of contingent assets and liabilities. On an ongoing basis, management evaluates these estimates and judgments, including those related to revenue recognition, valuation of inventory and accounts receivable, valuation of investments and income taxes, stock-based compensation, sabbatical leave, software development costs eligible for capitalization, goodwill, intangible assets and related amortization. The Company bases these estimates on historical and anticipated results and trends and on various other assumptions that the Company believes are reasonable under the circumstances, including assumptions as to future events. These estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. By their nature, estimates are subject to an inherent degree of uncertainty. Actual results may differ from management's estimates.

***Recent Pronouncements***

In December 2007, Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 141(R) *Business Combinations* ( SFAS 141R ). SFAS 141R establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree. SFAS 141R also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The guidance will become effective for fiscal years beginning after December 15, 2008. SFAS No. 141R is effective for the Company beginning February 1, 2009.

In December 2007, the FASB issued SFAS No. 160 *Noncontrolling Interests in Consolidated Financial Statements - an amendment of ARB No. 51* ( SFAS 160 ). SFAS 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. The guidance will become effective for fiscal years beginning after December 15, 2008. SFAS 160 is effective for us beginning February 1, 2009. The Company is currently assessing the impact that SFAS 160 may have on our results of operations and financial position.

In March 2008, the FASB issued FASB Statement No. 161 ( SFAS 161 ), *Disclosures about Derivative Instruments and Hedging Activities*. SFAS 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows. It is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. The Company is currently evaluating the impact of adopting SFAS 161 on its results of operations and financial position.

On May 9, 2008, the FASB issued FASB Statement No. 162, *The Hierarchy of Generally Accepted Accounting Principles* ( SFAS 162 ). The new standard is intended to improve financial reporting by identifying a consistent framework, or hierarchy, for selecting accounting principles to be used in preparing financial statements that are presented in conformity with U.S. generally accepted accounting principles ( GAAP ) for nongovernmental entities. Prior to the issuance of SFAS 162, GAAP hierarchy was defined for public accountants and their firms in the American Institute of Certified Public Accountants (AICPA) Statement on Auditing Standards (SAS) No. 69, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles* . SFAS 162 states that the GAAP hierarchy should be directed to entities because it is the entity (not its auditor) that is responsible for selecting accounting principles for financial statements that are presented in conformity with GAAP. SFAS 162 is effective 60 days following the Security Exchange Commission's approval of the Public Company Accounting Oversight Board Auditing amendments to AU Section 411, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles* . The adoption of SFAS 162 is not expected to have a material impact on the Company's position.

On December 12, 2007, the FASB ratified Emerging Issues Task Force ( EITF ) Issue No. 07-01, *Accounting for Collaborative Arrangements* ( EITF 07-01 ). EITF 07-01 defines collaborative arrangements and establishes reporting requirements for transactions between participants in a collaborative arrangement and between participants in the arrangement and third parties. EITF 07-01 also establishes the appropriate income statement presentation and classification for joint operating activities and payments between participants, as well as the sufficiency of the disclosures related to these arrangements. EITF 07-01 is effective for fiscal years beginning after December 15, 2008 (February 1, 2009, for the Company). Companies are required to apply EITF 07-01 using a modified version of retrospective transition for those

**Table of Contents**

arrangements in place at the effective date. In addition, companies are required to report the effects of the application of EITF 07-01 as a change in accounting principle through retrospective application to all prior periods presented for all arrangements existing as of the effective date, unless it is impracticable to apply the effects of the change retrospectively. We are currently assessing the impact that EITF 07-01 may have on our results of operations and financial position.

On April 25, 2008, the FASB issued FASB Staff Position ( FSP ) FAS 142-3, *Determination of the Useful Life of Intangible Assets*, which revises the factors that an entity should consider to develop renewal or extension assumptions used in determining the useful life of a recognized intangible asset. The FSP amends paragraph 11(d) of SFAS 142. The FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008 (February 1, 2009, for the Company) and for interim periods within those fiscal years. Early adoption is prohibited. Entities should apply the FSP's guidance on determining the useful life of an intangible asset prospectively to recognized intangible assets acquired after the FSP's effective date. However, once effective, the FSP's disclosure requirements apply prospectively to all recognized intangible assets, including those acquired before the FSP's effective date. We are currently assessing the impact that FAS 142-3 may have on our results of operations and financial position.

***Impact of the Recently Adopted Accounting Pronouncements***

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurement* ( SFAS 157 ). SFAS 157 defines fair value, establishes a framework for measuring fair value using generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement does not require any new fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. Effective February 1, 2008 the Company has made additional disclosures upon the adoption of SFAS 157 regarding fair valuation of its investments for our available-for-sale marketable securities. The impact of this adoption did not materially affect the Company's results of operations and financial position.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ( SFAS 159 ). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The impact of this adoption did not materially affect the Company's results of operations and financial position.

**ITEM 3. Quantitative and Qualitative Disclosures About Market Risk**

We face exposure to financial market risks, including adverse movements in foreign currency exchange rates and changes in interest rates. These exposures may change over time as business practices evolve and could have a material adverse impact on our financial results. Our foreign currency exchange exposure is primarily associated with product sales arrangements, European and Asian repatriation or settlement of intercompany payables and receivables among subsidiaries and its parent company, and/or investment/equity contingency considerations denominated in the local currency where the functional currency of the foreign subsidiary is the U.S. dollar. Substantially all of our product international sales are payable in United States Dollars (USD) or in the case of our ODG operations, service sales, payable in GBP, and provide a natural hedge for receipts and local payments. In light of the high proportion of our international businesses we expect the risk of any adverse movements in foreign currency exchange rates to have a greater impact on our translated results within the income statement and equity section of our balance sheet. Historically, we have not hedged specific currency exposures as gains and losses on foreign currency transactions have not been material to date. At April 30, 2008 and January 31, 2008, we had no variable rate U.S. dollar denominated debt. As there were no amounts outstanding at April 30, 2008 and January 31, 2008 related to variable rate debt, there was no interest rate exposure.

The carrying amounts reflected in the condensed consolidated balance sheet of cash and cash equivalents, short-term marketable securities, trade receivables and trade payables approximate fair value at April 30, 2008 due to the short maturities of these instruments. We maintain investment portfolio holdings of various issuers, types, and maturities. Our cash and marketable securities include cash equivalents, which we consider to be investments purchased with original maturities of three months or less. Given the short maturities and investment grade quality of the portfolio holdings at April 30, 2008, a sharp rise in interest rates should not have a material adverse impact on the fair value of our investment portfolio. Additionally, our long term marketable investments, which are carried at the lower of cost or market, have fixed interest rates, and therefore are subject to changes in fair value. As a result, we do not currently hedge these market risk exposures. At April 30, 2008, we had \$20.1 million in short-term marketable securities and \$6.7 million in long-term marketable securities.



**Table of Contents**

**ITEM 4. Controls and Procedures**

(a) *Evaluation of disclosure controls and procedures.* The Company evaluated the effectiveness of our disclosure controls and procedures, as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended (the Exchange Act ), as of the end of the period covered by this quarterly report on Form 10-Q. William C. Styslinger, III, our Chief Executive Officer, and Kevin M. Bisson, our Chief Financial Officer, reviewed and participated in this evaluation. Based upon that evaluation, Messrs. Styslinger and Bisson concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report and as of the date of the evaluation

(b) *Changes in internal controls over financial reporting* As a result of the evaluation completed by the Company, and in which Messrs. Styslinger and Bisson participated, the company has concluded that there were no changes during the fiscal quarter ended April 30, 2008 in our internal controls over financial reporting, which have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.



---

**Table of Contents**

**PART II. OTHER INFORMATION**

**ITEM 1. Legal Proceedings  
Litigation**

None.

**Other Matters**

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

SeaChange enters into agreements in the ordinary course of business with customers, resellers, distributors, integrators and suppliers. Most of these agreements require SeaChange to defend and/or indemnify the other party against intellectual property infringement claims brought by a third party with respect to SeaChange's products. From time to time, SeaChange also indemnifies customers and business partners for damages, losses and liabilities they may suffer or incur relating to personal injury, personal property damage, product liability, and environmental claims relating to the use of SeaChange's products and services or resulting from the acts or omissions of SeaChange, its employees, authorized agents or subcontractors. For example, SeaChange has received requests from several of its customers for indemnification of patent litigation claims asserted by Acacia Media Technologies, USA Video Technology Corporation and VTran Media Technologies. Management performed an analysis of all requests under Statement of Financial Accounting Standards No. 5, *Accounting for Contingencies* ( SFAS 5 ) and determined that as of January 31, 2008 \$148,000 was estimable and probable and has recorded an accrual.

SeaChange warrants that its products, including software products, will substantially perform in accordance with its standard published specifications in effect at the time of delivery. Most warranties have at least a one year duration that generally commence upon installation. In addition, SeaChange provides maintenance support to all customers and therefore allocates a portion of the product purchase price to the initial warranty period and recognizes revenue on a straight line basis over that warranty period related to both the warranty obligation and the maintenance support agreement. When SeaChange receives revenue for extended warranties beyond the standard duration, it is deferred and recognized on a straight line basis over the contract period. Related costs are expensed as incurred.

In the ordinary course of business, SeaChange provides minimum purchase guarantees to certain of its vendors to ensure continuity of supply against the market demand. Although some of these guarantees provide penalties for cancellations and/or modifications to the purchase commitments as the market demand decreases, most of the guarantees do not. Therefore, as the market demand decreases, SeaChange re-evaluates the accounting implications of guarantees and determines what charges, if any, should be recorded.

With respect to its agreements covering product, business or entity divestitures and acquisitions, SeaChange provides certain representations and warranties and agrees to indemnify and hold such purchasers harmless against breaches of such representations, warranties and covenants. Many of the indemnification claims have a definite expiration date while some remain in force indefinitely. With respect to its acquisitions, SeaChange may, from time to time, assume the liability for certain events or occurrences that took place prior to the date of acquisition.

SeaChange provides such guarantees and indemnification obligations after considering the economics of the transaction and other factors including but not limited to the liquidity and credit risk of the other party in the transaction. SeaChange believes that the likelihood is remote that any such arrangement could have a material adverse effect on its financial position, results of operation or liquidity. SeaChange records liabilities, as disclosed above, for such guarantees based on the Company's best estimate of probable losses which considers amounts recoverable under any recourse provisions.

**Table of Contents****ITEM 1A. Risk Factors**

In addition to the other information set forth in this Form 10-Q, you should carefully consider the risk factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended January 31, 2008, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks that we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition or future results.

**ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds***Repurchase of the Company's Equity Securities*

On February 13, 2008, SeaChange International's Board of Directors authorized the repurchase of up to \$20.0 million of its common stock, par value \$.01 per share, through a share repurchase program. As authorized by the program, shares may be purchased in the open market or through privately negotiated transactions, in a manner consistent with applicable securities laws and regulations, including pursuant to Rule 10b5-1 plan maintained by the Company. This stock repurchase program does not obligate the Company to acquire any specific number of shares and may be suspended or discontinued at any time. All repurchases are expected to be funded from the Company's current cash and investments balances. The Company does not intend to repurchase any shares from its management team or other insiders. The following table below provides monthly activity for the number of shares the Company has acquired and its average price paid per share, net of broker fees, during the first quarter of fiscal 2009.

**PURCHASES OF EQUITY SECURITIES**

Period	Total Number of Shares (or Units) Purchased	Average Price Paid per Share (Or Units) (1)	Total Number of Shares (Or Units) Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares (Or Units) that May Yet Be Purchased Under the Plans or Programs
February 1, 2008 to February 29, 2008		\$		\$ 20,000,000
March 1, 2008 to March 31, 2008	79,464	\$ 6.90	79,464	\$ 19,450,554
April 1, 2008 to April 30, 2008	203,211	\$ 7.03	203,211	\$ 18,018,400
Total	282,675	\$ 7.01	282,675	

(1) net of broker fees.

The repurchase program is scheduled to terminate on December 31, 2008, and may be modified or discontinued at any time. As of April 30, 2008, 282,675 shares of our common stock had been purchased as part of the repurchase program at an average price of \$7.01. As of April 30, 2008, the remaining maximum dollar value of shares that may yet be purchased under the program is \$18.0 million.

**ITEM 6. Exhibits**

(a) Exhibits

## Edgar Filing: SEACHANGE INTERNATIONAL INC - Form 10-Q

Certification Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

31.2 Certification Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).

32.2 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).

**Table of Contents**

**SIGNATURES**

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

Dated: June 9, 2008

**SEACHANGE INTERNATIONAL, INC.**

by: **/s/ KEVIN M. BISSON**  
**Kevin M. Bisson**  
**Chief Financial Officer,**

**Senior Vice President, Finance and**

**Administration, Treasurer and Secretary**

**Index to Exhibits**

<b>No.</b>	<b>Description</b>
31.1	Certification Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31.2	Certification Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.1	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
32.2	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).