VEEVA SYSTEMS INC
Form 10-Q
June 07, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended April 30, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to .

Commission File Number: 001-36121

Veeva Systems Inc.

(Exact name of registrant as specified in its charter)

Delaware	20-8235463
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

4280 Hacienda Drive

Pleasanton, California 94588
(Address of principal executive offices) (Zip Code)

(Registrant's telephone number, including area code) (925) 452-6500

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

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

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

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

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
Emerging growth company		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of May 31, 2018, there were 120,613,021 shares of the Registrant's Class A common stock outstanding and 22,826,092 shares of the Registrant's Class B common stock outstanding.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements that are based on our beliefs and assumptions and on information currently available to us. Forward-looking statements include information concerning our possible or assumed future results of operations and expenses, business strategies and plans, trends, market sizing, competitive position, industry environment, potential growth opportunities and product capabilities, among other things. Forward-looking statements include all statements that are not historical facts and, in some cases, can be identified by terms such as “aim,” “anticipates,” “believes,” “could,” “estimates,” “expects,” “goal,” “intends,” “may,” “plans,” “potential,” “predicts,” “projects,” “strive,” “will,” “would” or similar expressions and the negatives of those terms.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements, including those described in “Risk Factors,” “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and elsewhere in this report. Given these uncertainties, you should not place undue reliance on these forward-looking statements.

Any forward-looking statement made by us in this report speaks only as of the date on which it is made. Except as required by law, we disclaim any obligation to update these forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future.

As used in this report, the terms “Veeva,” the “Company,” “Registrant,” “we,” “us,” and “our” mean Veeva Systems Inc. and its subsidiaries unless the context indicates otherwise.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.
VEEVA SYSTEMS INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except number of shares and par value)

	April 30, 2018 (Unaudited)	January 31, 2018 *As adjusted
Assets		
Current assets:		
Cash and cash equivalents	$460,239	$320,183
Short-term investments	458,069	441,779
Accounts receivable, net of allowance for doubtful accounts of $538 and $345, respectively	154,840	224,668
Unbilled accounts receivable	17,635	13,348
Prepaid expenses and other current assets	12,045	12,443
Total current assets	1,102,828	1,012,421
Property and equipment, net	51,500	52,284
Deferred costs, net	29,338	30,306
Goodwill	95,804	95,804
Intangible assets, net	29,644	31,490
Deferred income taxes, noncurrent	2,189	2,222
Other long-term assets	6,352	5,806
Total assets	$1,317,655	$1,230,333
Liabilities and stockholders’ equity		
Current liabilities:		
Accounts payable	$9,023	$6,944
Accrued compensation and benefits	15,380	17,054
Accrued expenses and other current liabilities	12,263	13,152
Income tax payable	—	2,080
Deferred revenue	289,560	266,939
Total current liabilities	326,226	306,169
Deferred income taxes, noncurrent	9,737	10,949
Other long-term liabilities	7,255	6,977
Total liabilities	343,218	324,095
Commitments and contingencies (Note 12)		
Stockholders’ equity:		
Class A common stock, $0.00001 par value; 800,000,000 shares authorized,	1	1

120,368,510 and 117,246,735 issued and outstanding at April 30, 2018 and January 31, 2018, respectively		
Class B common stock, $0.00001 par value; 190,000,000 shares authorized, 22,808,075 and 24,822,661 issued and outstanding at April 30, 2018 and January 31, 2018, respectively	—	—
Additional paid-in capital	539,665	515,272
Accumulated other comprehensive income	1,096	1,600
Retained earnings	433,675	389,365
Total stockholders' equity	974,437	906,238
Total liabilities and stockholders' equity	$ 1,317,655	$ 1,230,333

See Notes to Condensed Consolidated Financial Statements.

*See note 1 of the notes to the condensed consolidated financial statements for a summary of adjustments.

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VEEVA SYSTEMS INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands, except per share data)

	Three months ended April 30, 2018	2017 *As adjusted
	(Unaudited)	
Revenues:		
Subscription services	$156,003	$129,131
Professional services and other	39,544	30,641
Total revenues	195,547	159,772
Cost of revenues(1):		
Cost of subscription services	29,913	26,138
Cost of professional services and other	30,242	22,739
Total cost of revenues	60,155	48,877
Gross profit	135,392	110,895
Operating expenses(1):		
Research and development	37,197	28,311
Sales and marketing	34,385	30,141
General and administrative	19,854	13,580
Total operating expenses	91,436	72,032
Operating income	43,956	38,863
Other income, net	2,139	591
Income before income taxes	46,095	39,454
Provision for income taxes	1,785	2,458
Net income	$44,310	$36,996
Net income attributable to Class A and Class B common stockholders, basic and diluted	$44,310	$36,996
Net income per share attributable to Class A and Class B common stockholders:		
Basic	$0.31	$0.27
Diluted	$0.29	$0.24
Weighted-average shares used to compute net income per share attributable to Class A and Class B common stockholders:		

Basic	142,777	137,096
Diluted	154,935	151,056
Other comprehensive income:		
Net change in unrealized losses on available-for-sale investments	$305	$(106)
Net change in cumulative foreign currency translation gain	(809)	905
Comprehensive income	$43,806	$37,795

(1) Includes stock-based compensation as follows:

Cost of revenues:		
Cost of subscription services	$345	$342
Cost of professional services and other	2,328	1,689
Research and development	4,667	3,802
Sales and marketing	4,088	3,847
General and administrative	5,583	2,108
Total stock-based compensation	$17,011	$11,788

See Notes to Condensed Consolidated Financial Statements.

* See note 1 of the notes to the condensed consolidated financial statements for a summary of adjustments.

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VEEVA SYSTEMS INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Three months ended April 30, 2018 (Unaudited)	2017 * As adjusted
Cash flows from operating activities		
Net income	$44,310	$36,996
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,596	3,449
Amortization of premiums (accretion of discount) on short-term investments	(179)	456
Stock-based compensation	17,011	11,788
Amortization of deferred costs	4,519	4,048
Deferred income taxes	(50)	(647)
Loss on foreign currency from market-to-market derivative	23	49
Bad debt expense	236	(8)
Changes in operating assets and liabilities:		
Accounts receivable	69,592	70,804
Unbilled accounts receivable	(4,287)	(7,932)
Deferred costs	(3,551)	(3,717)
Income taxes	(2,496)	(2,545)
Prepaid expenses and other current and long-term assets	(713)	(1,491)
Accounts payable	1,981	(456)
Accrued expenses and other current liabilities	(2,564)	905
Deferred revenue	22,650	29,411
Other long-term liabilities	507	1,051
Net cash provided by operating activities	150,585	142,161
Cash flows from investing activities		
Purchases of short-term investments	(193,162)	(56,249)
Maturities and sales of short-term investments	176,544	58,696
Purchases of property and equipment	(709)	(3,960)
Capitalized internal-use software development costs	(230)	(791)
Net cash used in investing activities	(17,557)	(2,304)
Cash flows from financing activities		
Proceeds from exercise of common stock options	7,839	7,285
Net cash provided by financing activities	7,839	7,285

Effect of exchange rate changes on cash, cash equivalents, and restricted cash	(811)	913
Net change in cash, cash equivalents, and restricted cash	140,056	148,055
Cash, cash equivalents, and restricted cash at beginning of period	321,387	218,607
Cash, cash equivalents, and restricted cash at end of period	$461,443	$366,662
Cash, cash equivalents, and restricted cash at end of period:		
Cash and cash equivalents	$460,239	$365,660
Restricted cash included in other long-term assets	1,204	1,002
Total cash, cash equivalents, and restricted cash at end of period	$461,443	$366,662
Supplemental disclosures of other cash flow information:		
Cash paid for income taxes, net of refunds	$4,116	$4,256
Excess tax benefits from employee stock plans	$9,679	$13,910
Non-cash investing and financing activities:		
Changes in accounts payable and accrued expenses related to property and equipment purchases	$99	$(586)
Vesting of early exercised stock options	$—	$1

See Notes to Condensed Consolidated Financial Statements.

*See note 1 of the notes to the condensed consolidated financial statements for a summary of adjustments.

VEEVA SYSTEMS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Summary of Business and Significant Accounting Policies

Description of Business

Veeva is a leading provider of industry cloud solutions for the global life sciences industry. We were founded in 2007 on the premise that industry-specific cloud solutions could best address the operating challenges and regulatory requirements of life sciences companies. Our products are designed to meet the unique needs of our customers and their most strategic business functions—from research and development (R&D) to commercialization. Our products address a broad range of needs—including multichannel customer relationship management (CRM), content management, master data management, and data regarding healthcare professionals and organizations. Veeva is also offering its regulated content management solutions to a new set of customers in process and discrete manufacturing, consumer packaged goods, and highly regulated services industries. Our fiscal year end is January 31.

Principles of Consolidation and Basis of Presentation

These unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting and include the accounts of our wholly-owned subsidiaries after elimination of intercompany accounts and transactions. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in Veeva’s Annual Report on Form 10-K for the fiscal year ended January 31, 2018, filed on March 29, 2018. Except for the accounting policies for revenue recognition, unbilled accounts receivable, and deferred costs that were updated as a result of adopting ASU 2014-09, “Revenue from Contracts with Customers” (Topic 606), there have been no changes to our significant accounting policies described in the annual report that have had a material impact on our condensed consolidated financial statements and related notes.

The condensed consolidated balance sheet as of January 31, 2018 included herein was derived from the audited financial statements as of that date. These unaudited condensed consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial position, results of operations, our comprehensive income and cash flows for the interim periods, but are not necessarily indicative of the results of operations to be anticipated for the full fiscal year ending January 31, 2019 or any other period.

Effective February 1, 2018, we adopted the requirements of Topic 606, ASU 2016-18, “Statement of Cash Flows, Restricted Cash,” and ASU 2018-02, “Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income,” as discussed in this note. All amounts and disclosures set forth in this Form 10-Q for previously reported periods have also been updated to comply with the new standards, as indicated by the “as adjusted” tables in this footnote.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with GAAP requires us to make estimates, judgments and assumptions that affect the condensed consolidated financial statements and the notes thereto. These estimates are based on information available as of the date of the condensed consolidated financial statements. On a regular basis, management evaluates these estimates and assumptions. Significant items subject to such estimates and assumptions include, but are not limited to:

- the standalone selling price for each distinct performance obligation included in customer contracts with multiple performance obligations;
- the period of benefit for deferred costs;
- the collectibility of our accounts receivable;
- the fair value of assets acquired and liabilities assumed for business combinations;
- the valuation of short-term investments and the determination of other-than-temporary impairments;

- the realizability of deferred income tax assets and liabilities;
- the fair value of our stock-based awards; and
- the capitalization and estimated useful life of internal-use software development costs.

As future events cannot be determined with precision, actual results could differ significantly from those estimates.

Revenue Recognition

We derive our revenues primarily from subscription services and professional services. Subscription services revenues consist of fees from customers accessing our cloud-based software solutions and subscription or license fees for our data solutions. Professional services and other revenues consist primarily of fees from implementation services, configuration, data services, training and managed services related to our solutions. Revenues are recognized when control of these services is transferred to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for those services.

We determine revenue recognition through the following steps:

- Identification of the contract, or contracts, with a customer;
- Identification of the performance obligations in the contract;
- Determination of the transaction price;
- Allocation of the transaction price to the performance obligations in the contract; and
- Recognition of revenue when, or as, we satisfy a performance obligation.

Our subscription services agreements are generally non-cancelable during the term, although customers typically have the right to terminate their agreements for cause in the event of material breach.

Subscription Services Revenues

Subscription services revenues are recognized ratably over the respective non-cancelable subscription term because of the continuous transfer of control to the customer. Our subscription arrangements are considered service contracts, and the customer does not have the right to take possession of the software.

Professional Services and Other Revenues

The majority of our professional services arrangements are recognized on a time and materials basis. Professional services revenues recognized on a time and materials basis are measured monthly based on time incurred and contractually agreed upon rates. Certain professional services revenues are based on fixed fee arrangements and revenues are recognized as services are rendered. Data services and training revenues are generally recognized as the services are performed.

Contracts with Multiple Performance Obligations

Some of our contracts with customers contain multiple performance obligations. For these contracts, we account for individual performance obligations separately if they are distinct. The transaction price is allocated to the separate performance obligations on a relative standalone selling price basis. We determine the standalone selling prices based on our overall pricing objectives, taking into consideration market conditions and other factors, including other groupings such as customer type and geography.

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Unbilled Accounts Receivable

Unbilled accounts receivable is a contract asset related to the delivery of our subscription services and professional services for which the related billings will occur in a future period. Unbilled accounts receivable consists of (i) revenue recognized for professional services performed but yet not billed and (ii) revenue recognized from non-cancelable, multi-year orders in which fees increase annually but for which we are not contractually able to invoice until a future period.

Deferred Costs

Deferred costs include sales commissions associated with obtaining a contract with a customer. These costs are deferred and then amortized over a period of benefit that we have determined to be three years. We determined the period of benefit by taking into consideration our customer contracts, our technology and other factors. Amortization expense is included in sales and marketing expenses in the accompanying condensed consolidated statements of operations.

Deferred Revenue

Deferred revenue includes amounts billed to customers for which the revenue recognition criteria have not been met. Deferred revenue primarily consists of billings or payments received in advance of revenue recognition from our subscription services and, to a lesser extent, professional services and other revenues described above. Deferred revenue is recognized as we satisfy our performance obligations. We generally invoice our customers in annual or quarterly installments for subscription services. Accordingly, the deferred revenue balance does not generally represent the total contract value of a subscription arrangement. Deferred revenue that will be recognized during the succeeding 12-month period is recorded as current deferred revenue and the remaining portion is recorded as noncurrent, which is included in other long-term liabilities on the condensed consolidated balance sheet.

Certain Risks and Concentrations of Credit Risk

Our revenues are derived from subscription services, professional services and other services delivered primarily to the life sciences industry. We operate in markets that are highly competitive and rapidly changing. Significant technological changes, shifting customer needs, the emergence of competitive products or services with new capabilities and other factors could negatively impact our operating results.

Our financial instruments that potentially subject us to concentration of credit risk consist primarily of cash and cash equivalents, short-term investments and trade accounts receivable. Our cash equivalents and short-term investments are held by established financial institutions. We have established guidelines relative to credit ratings, diversification and maturities that seek to maintain safety and liquidity. Deposits in these financial institutions may significantly exceed federally insured limits.

We do not require collateral from our customers and generally require payment within 30 to 60 days of billing. We periodically evaluate the collectibility of our accounts receivable and provide an allowance for doubtful accounts as necessary, based on historical experience. Historically, losses related to lack of collectibility have not been material.

The following customers individually exceeded 10% of total accounts receivable as of the dates shown:

	April 30, 2018	January 31, 2018
Customer 1	*	18%
Customer 2	*	13%
Customer 3	15%	*
Customer 4	12%	*

*Does not exceed 10%.
No single customer represented over 10% of total revenues in the condensed consolidated statements of comprehensive income for the three months ended April 30, 2018 and 2017.

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New Accounting Pronouncements Adopted in Fiscal 2019

Stranded Tax Effects in Accumulated Other Comprehensive Income

In February 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2018-02, "Income Statement-Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." This update allows reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017 (Tax Act).

ASU 2018-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those years. We early adopted this standard effective February 1, 2018. The impact on our condensed consolidated financial statements was immaterial.

Restricted Cash

In November 2016, the FASB issued ASU 2016-18, “Statement of Cash, Restricted Cash,” which requires that amounts generally described as restricted cash or restricted cash equivalents be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. This standard is effective for our interim and annual reporting periods beginning after December 15, 2017. We adopted ASU 2016-18 retrospectively, effective February 1, 2018. As a result of including restricted cash with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts presented on the condensed consolidated statement of cash flows, the impact on net cash flows for the three months ended April 30, 2018 was not material.

Financial Instruments

In January 2016, the FASB issued ASU 2016-01, “Financial Instruments.” ASU 2016-01, among other things, requires equity investments, with certain exceptions, to be measured at fair value with changes in fair value recognized in net income and clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity’s other deferred tax assets. This standard is effective for our interim and annual reporting periods beginning after December 15, 2017. We adopted ASU 2016-01 effective February 1, 2018. There was no impact to our condensed consolidated financial statements.

Revenue Recognition

In May 2014, the FASB issued Topic 606. This guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model requires revenue to be recognized when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. Topic 606 supersedes the existing revenue recognition guidance in “Revenue Recognition (Topic 605)”.

We have adopted the requirements of the new standard as of February 1, 2018, utilizing the full retrospective transition method. Adoption of the new standard resulted in changes to our accounting policies for revenue recognition, unbilled accounts receivable, and deferred costs as detailed above in our description of Revenue Recognition. We applied a practical expedient provided by the new standard and are not disclosing the amount of consideration allocated to the remaining performance obligations for all reporting periods presented before the date of the initial application.

The impact of adoption included the deferral of costs to obtain customer contracts, which is comprised of commissions on our subscription services arrangements and the other associated fringe benefits. Such costs were expensed as incurred under Topic 605, whereas under Topic 606, they are generally capitalized and amortized over the costs’ associated term of economic benefit. We have determined that the term of economic benefit of our costs to obtain customer contracts is three years.

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Revenue for the majority of our subscription services customer contracts will continue to be recognized over time because of the continuous transfer of control to the customer; however, there is some impact to revenue primarily driven by (i) accounting for non-cancelable multi-year contracts, (ii) the removal of the current limitation on contingent revenue, which may result in revenue being recognized earlier for certain contracts, and (iii) allocation of revenue from subscription services to professional services.

We adjusted our condensed consolidated financial statements from amounts previously reported to reflect the adoption of Topic 606, ASU 2016-18 and ASU 2018-02. Select impacted condensed consolidated balance sheet line items, which reflect the adoption of the new standards are as follows (in thousands):

	January 31, 2018		
	As Reported	Adjustments	As adjusted
Assets			
Accounts receivable[1]	$233,731	(9,063)a	$224,668
Unbilled accounts receivable[1]	—	13,348 a	13,348
Deferred costs, net	—	30,306 a	30,306
Deferred income taxes, non-current	3,490	(1,268)a	2,222
Liabilities			
Deferred revenue	$275,446	$ (8,507)a	$266,939
Deferred income taxes, non-current	3,828	7,121 a	10,949
Stockholders' equity:			