VIALTA INC
Form 10-Q
May 15, 2002

**Table of Contents**

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2002.

OR

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

For the transition period from: ___________ to: __________ .

Commission file number 0-32809

VIALTA, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

| | |
|---|---|
| Delaware<br>(State or Other Jurisdiction of Incorporation or Organization) | 94-3337326<br>(I.R.S. Employer Identification No.) |

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

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

Indicate by check whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes [ ] No [X]

The number of outstanding shares of the registrant s Class A common stock, par value $0.001 per share, on April 23, 2002 was 43,010,959 shares. The number of outstanding shares of the registrant s Class B common stock, par value $0.001 per share, on April 23, 2002 was 40,580,375 shares.

**TABLE OF CONTENTS**

**Table of Contents**

VIALTA, INC.

TABLE OF CONTENTS

**Table of Contents**

**PART I. FINANCIAL INFORMATION**

**ITEM 1: FINANCIAL STATEMENTS**

**VIALTA, INC.**
**(A Development Stage Company)**
**CONDENSED CONSOLIDATED BALANCE SHEETS**
**(unaudited)**

| | March 31, 2002 | December 31, 2001 |
|---|---|---|
| | (in thousands) | |
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 49,970 | $ 61,886 |
| Short-term investments | 9,459 | 5,542 |
| Prepaid expenses and other current assets | 3,193 | 2,989 |
| Total current assets | 62,622 | 70,417 |
| Property and equipment, net | 6,307 | 7,831 |
| Long term investments and other assets | 84 | 4,276 |
| Content licenses | 6,131 | 1,342 |
| Total assets | $ 75,144 | $ 83,866 |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 682 | $ 760 |
| Accrued expenses and other current liabilities | 2,981 | 2,827 |
| Total current liabilities | 3,663 | 3,587 |
| Stockholders equity: | | |
| Common stock | 93 | 92 |
| Additional paid-in capital | 144,096 | 144,164 |
| Deficit accumulated during the development stage | (66,626) | (60,087) |
| Accumulated other comprehensive income | 66 | 156 |
| Treasury stock | (6,148) | (4,046) |
| Total stockholders equity | 71,481 | 80,279 |
| Total liabilities and stockholders equity | $ 75,144 | $ 83,866 |

*See accompanying notes to the condensed consolidated financial statements.*

Table of Contents

**VIALTA, INC.**
**(A Development Stage Company)**
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**
**(unaudited)**

| | Three months ended March 31, 2002 | Three months ended March 31, 2001 | Period from April 20, 1999 (Date of of Inception) Through March 31, 2002 |
|---|---|---|---|
| | (in thousands, except per share data) | | |
| Operating expenses: | | | |
| Research and development | $ 4,223 | $ 4,528 | $ 50,400 |
| Amortization of content licenses | 253 | | 253 |
| Sales and marketing | 614 | 995 | 7,941 |
| General and administrative | 1,812 | 2,357 | 18,322 |
| Operating loss | (6,902) | (7,880) | (76,916) |
| Interest income, net | 363 | 1,230 | 12,169 |
| Other expenses | | (19) | (2,939) |
| Loss before income tax benefit | (6,539) | (6,669) | (67,686) |
| Income tax benefit | | | 1,060 |
| Net loss | $ (6,539) | $ (6,669) | $ (66,626) |
| Net loss per share: | | | |
| Basic and diluted | $ (0.08) | $ (1.07) | $ (2.74) |
| Weighted average common shares outstanding | 85,240 | 6,231 | 24,297 |

*See accompanying notes to the condensed consolidated financial statements.*

**Table of Contents**

**VIALTA, INC.**
**(A Development Stage Company)**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(unaudited)**

| | Three months ended March 31, 2002 | Three months ended March 31, 2001 | Period from April 20, 1999 (Date of Inception) Through March 31, 2002 |
|---|---|---|---|
| | | (in thousands) | |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net loss | $ (6,539) | $ (6,669) | $ (66,626) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | | |
| Depreciation and amortization | 1,818 | 1,235 | 11,544 |
| Amortization of content license fees | 253 | | 253 |
| Write-down of long-term investment | | | 2,750 |
| Changes in assets and liabilities: | | | |
| Inventories | | (504) | |
| Prepaid expenses and other current assets | (204) | 1,177 | (3,116) |
| Accounts payable and accrued liabilities | (1) | 95 | 3,586 |
| Net cash used in operating activities | (4,673) | (4,666) | (51,609) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | |
| Purchase of available-for-sale investments | | | (136,776) |
| Proceeds from maturity and sale of available-for-sale investments | 57 | 27,112 | 127,383 |
| Purchase of long-term investments | | (2,000) | (6,100) |
| Purchase of content licenses | (5,042) | (231) | (6,384) |
| Acquisition of property and equipment | (166) | (1,584) | (14,585) |
| Net cash provided by (used in) investing activities | (5,151) | 23,297 | (36,462) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | | |
| Repayment of notes payable to related party | | (30,000) | |
| Proceeds from issuance of redeemable convertible preferred stock | | | 142,600 |
| Proceeds from issuance of common stock | 10 | | 1,589 |
| Repurchase of common stock | (2,102) | | (6,148) |
| Net cash provided by (used in) financing activities | (2,092) | (30,000) | 138,041 |
| Net increase in cash and cash equivalents | (11,916) | (11,369) | 49,970 |
| Cash and cash equivalents, beginning of the period | 61,886 | 109,378 | |
| Cash and cash equivalents, end of the period | $ 49,970 | $ 98,009 | $ 49,970 |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION AND NONCASH FINANCING ACTIVITY: | | | |
| Cash paid for interest | $ | $ 194 | $ 194 |

| | | | |
|---|---|---|---|
| Issuance of note receivable in connection with issuance of common stock | $ — | $ — | $ 1,475 |

*See accompanying notes to the condensed consolidated financial statements.*

Table of Contents

**VIALTA, INC.**
**(A Development Stage Company)**
**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(unaudited)**

**NOTE 1. THE COMPANY**

Vialta, Inc. ( Vialta or the Company ) was incorporated in California on April 20, 1999 and reincorporated in the State of Delaware on April 20, 2001. Vialta has developed a multi-purpose DVD player ( ViDVD ) that offers Internet access and other features, such as CD, MP3, karaoke, and support for other audio and video formats. These features differentiate it from most DVD players currently available in the U.S. consumer market. This ViDVD player is the first product offering from Vialta s digital home entertainment platform, which the Company anticipates will grow to support a family of multimedia Internet appliances. Vialta commenced shipments of the ViDVD through retail distribution channels in the third quarter of 2001. The Company is also developing a videophone converter, known as Beamer™, that will allow consumers to transform their standard phone into a videophone, delivering a live motion color video picture over regular phone lines at no additional cost to a regular call.

Since its inception, Vialta has been in the development stage, and has incurred substantial losses and negative cash flows from operations in every fiscal period since inception. For the cumulative period ended March 31, 2002, Vialta incurred a loss from operations of approximately $76.9 million and negative cash flows from operations of $51.6 million. Management expects operating losses and negative cash flows to continue for the foreseeable future and anticipates that losses will increase significantly from current levels because of additional costs and expenses related to marketing activities, continued expansion of operations, continued development of Vialta s web site and information technology infrastructure, expansion of product offerings and development of relationships with other businesses. Management believes that Vialta has sufficient cash, cash equivalents, and short term investments to fund its development and growth through March 31, 2003. However, in the longer term, failure to generate sufficient revenues, raise additional capital or reduce certain discretionary spending could have a material adverse effect on Vialta s ability to achieve its intended business objectives.

**NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States of America ( GAAP ) have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the unaudited interim financial statements reflect only those normal recurring adjustments necessary for a fair statement of the financial position, operating results and cash flows of the Company for the periods presented. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2001 and the period from April 20, 1999 (date of inception) through December 31, 2001, included in the Company s Annual Report on Form 10-K filed on March 27, 2002. The results of operation for the three months ended March 31, 2002 are not necessarily indicative of the results that may be expected for any other periods or for the fiscal year ending December 31, 2002.

**Interim unaudited information**

Preparing the Company s financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the close of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

**Reclassifications**

Certain prior year balances have been reclassified to conform to the current financial statement presentation.

**Comprehensive Income (Loss)**

Statement of Financial Accounting Standards No. 130, Reporting Comprehensive Income ( SFAS 130 ) establishes standards for the reporting and display of comprehensive income and its components in financial statements. Comprehensive income, as defined, includes all changes in equity during a period from non-owner sources. The difference between net loss and comprehensive loss at March 31, 2002 was $90,000 related to unrealized losses on available-for-sale investments. Comprehensive loss for the three months ended March 31, 2002 was approximately $6,629,000. For the three months ended March 31, 2001, comprehensive loss approximated net loss.

**NOTE 3. RELATED PARTY TRANSACTIONS**

Effective August 1, 1999, the Company entered into a Research and Development Service Agreement with ESS whereby ESS provides certain research and development services to the Company in exchange for a service fee. In addition, the Company signed a reciprocal agreement with ESS whereby Vialta provides certain non-recurring expense services for the design and development of Internet related products and technologies to ESS in exchange for a service fee. In the periods presented, the Company did not provide such services to ESS.

Effective August 1, 1999, the Company entered into an Administrative and Management Service Agreement with ESS whereby ESS provides certain administrative and managerial services to Vialta including, without limitation, sales support, marketing support, production and logistical support, financial oversight, accounting assistance, contract review, personnel services (including training of employees) and such other general and administrative services as Vialta requires. ESS performs these services in consideration for a service fee. In addition, Vialta signed a reciprocal agreement whereby Vialta provides the services mentioned above to ESS in exchange for a service fee.

Effective August 1, 1999, the Company entered into a Purchase Agreement with ESS whereby Vialta will purchase certain products from ESS.

In January 2000, Vialta entered into an Assignment of Intellectual Property Agreement with ESS whereby Vialta paid ESS $2.0 million for the transfer of the Videophone and EnReach-based web browser technologies. Such transfer was done based on actual costs incurred. No fees were paid under this agreement for each of the three months ended March 31, 2002 and 2001.

In April 2000, Vialta loaned to an officer of Vialta $60,000, which, together with accrued interest at the annual rate of 6%, was due and payable on April 20, 2001. The loan, along with accrued interest, was repaid in August 2001.

On December 18, 2000, Vialta received a $30.0 million loan from a related party controlled by Annie M.H. Chan, a director of ESS and the spouse of Fred S.L. Chan, Chairman of ESS and Chairman and Chief Executive Officer of Vialta. The short-term loan along with approximately $194,000 accrued interest at 5.25% was repaid on January 31, 2001.

On August 20, 2001, Vialta re-executed the aforementioned existing agreements with ESS as a result of the spin-off of Vialta from ESS. Under the re-executed Administrative and Management Service Agreement, Vialta provided services to ESS in the amount of $102,600 for the three months ended March 31, 2002.

On August 20, 2001, Vialta entered into a Commercial Lease Agreement with ESS whereby ESS will lease a freestanding building in Fremont, California to Vialta for a fixed monthly fee. The lease expires on December 31, 2003.

On August 20, 2001, Vialta entered into an Employee Matters Agreement with ESS whereby Vialta will continue to provide employment and employee benefits to all active employees and former employees subject to certain limitations. No fees were paid under this agreement for each of the three months ended March 31, 2002 and 2001.

Table of Contents

The Company anticipates that it will continue to receive such services from ESS under the terms of the agreements. The following table summarizes the activities between the Company and ESS for the periods presented:

| | Three Months Ended March 31, | |
|---|---|---|
| | 2002 | 2001 |
| | (Amounts in thousands) | |
| Net receivables at beginning of period | $ 64 | $ 650 |
| Charges by Vialta to ESS: | | |
| Administrative & management service fees | 103 | |
| Spin-off related charges | 125 | |
| Payments made by Vialta on behalf of ESS | 79 | |
| Charges by ESS to Vialta | | |
| Research & development service fees | | (602) |
| Administrative & management service fees | (88) | (1,075) |
| Purchase agreement | (16) | (637) |
| Commercial lease agreement | (463) | |
| Cash receipts from ESS | (185) | (650) |
| Cash payments made to ESS | 480 | 1,982 |
| Net receivables (payables) at end of period | $ 99 | $ (332) |

**NOTE 4. BALANCE SHEET COMPONENTS**

| | March 31, 2002 | December 31, 2001 |
|---|---|---|
| | (Amounts in thousands) | |
| **Cash and Cash Equivalents** | | |
| Cash and money market funds, at cost which approximates fair value | $49,970 | $61,886 |
| **Marketable Securities** | | |
| U.S. Government debt securities | $ 4,242 | $ 4,274 |
| Corporate debt securities | 5,217 | 5,332 |
| | 9,459 | 9,606 |
| Due between one and two years | | 4,064 |
| Due within one year | $ 9,459 | $ 5,542 |
| **Property and Equipment** | | |
| Machinery and equipment | $ 7,305 | $ 7,149 |
| Furniture and fixtures | 607 | 607 |
| Software and web site development cost | 5,173 | 6,663 |
| | 13,085 | 14,419 |
| Less: Accumulated depreciation | (6,778) | (6,588) |

| | | |
|---|---|---|
| | $ 6,307 | $ 7,831 |
| **Long-term Investments and Other Assets** | | |
| Long-term investments in marketable securities | $ | $ 4,064 |
| Other investments | 38 | 166 |
| Deposit | 46 | 46 |
| | $ 84 | $ 4,276 |
| **Accrued Expenses and Other Current Liabilities** | | |
| Accrued compensation costs | $ 2,300 | $ 2,441 |
| Other | 681 | |