Wayside Technology Group, Inc.
Form 10-Q
November 07, 2018
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 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 No. 000-26408

Wayside Technology Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware	13-3136104
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

4 Industrial Way West, Suite 300, Eatontown, New Jersey 07724

(Address of principal executive offices)

(732) 389-8950

Registrant's Telephone Number

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 and 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 every Interactive Data File required to be submitted 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 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.

Check One:

Large Accelerated Filer	Accelerated Filer
	Smaller Reporting Company
Non-Accelerated Filer	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

There were 4,496,494 outstanding shares of common stock, par value $.01 per share (“Common Stock”) as of November 6, 2018, not including 788,006 shares classified as treasury stock.

Table of Contents

Wayside Technology Group, Inc. and Subsidiaries

Table of Contents

Table of Contents

PART I — FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

Wayside Technology Group, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(Unaudited)

(Amounts in thousands, except share and per share amounts)

	September 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 6,464	$ 5,530
Accounts receivable, net of allowances of $2,449 and $2,102, respectively	83,762	76,937
Inventory, net	1,760	2,794
Vendor prepayments	3,970	6,837
Prepaid expenses and other current assets	525	553
Total current assets	96,481	92,651
Equipment and leasehold improvements, net	1,682	1,828
Accounts receivable-long-term, net	4,535	7,437
Other assets	281	231
Deferred income taxes	131	138
	$ 103,110	$ 102,285
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 62,675	$ 62,792
Total current liabilities	62,675	62,792
Deferred rent and tenant allowances	729	781
Total liabilities	63,404	63,573
Stockholders' equity:		
	53	53

Common Stock, $.01 par value; 10,000,000 shares authorized; 5,284,500 shares issued: 4,498,223 and 4,454,829 shares outstanding, respectively		
Additional paid-in capital	32,241	31,257
Treasury stock, at cost, 786,277 and 829,671 shares, respectively	(13,426)	(14,207)
Retained earnings	22,020	22,522
Accumulated other comprehensive loss	(1,182)	(913)
Total stockholders' equity	39,706	38,712
	$ 103,110	$ 102,285

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

3

Table of Contents

Wayside Technology Group, Inc. and Subsidiaries

Condensed Consolidated Statements of Income

(Unaudited)

(Amounts in thousands, except per share data)

	Nine months ended September 30,		Three months ended September 30,	
	2018	2017	2018	2017
Net sales	$ 132,389	$ 116,130	$ 47,923	$ 39,018
Cost of sales	112,693	96,555	41,620	32,775
Gross profit	19,696	19,575	6,303	6,243
Selling, general, and administrative expenses	15,248	14,261	4,903	4,451
Separation expenses	2,446	—	—	—
Income from operations	2,002	5,314	1,400	1,792
Other income (expense):				
Interest, net	744	466	296	145
Foreign currency transaction gains	40	22	42	73
Income before provision for income taxes	2,786	5,802	1,738	2,010
Provision for income taxes	987	1,867	420	669
Net income	$ 1,799	$ 3,935	$ 1,318	$ 1,341
Income per common share-Basic	$ 0.40	$ 0.87	$ 0.29	$ 0.30
Income per common share-Diluted	$ 0.40	$ 0.87	$ 0.29	$ 0.30
Weighted average common shares outstanding — Basic	4,344	4,303	4,386	4,283
Weighted average common shares outstanding — Diluted	4,344	4,303	4,386	4,283

Dividends paid per common share	$ 0.51	$ 0.51	$ 0.17	$ 0.17

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

Table of Contents

Wayside Technology Group, Inc. and Subsidiaries

Condensed Consolidated Statements of Comprehensive Income (Loss)

(Unaudited)

(Amounts in thousands)

	Nine months ended September 30,		Three months ended September 30,	
	2018	2017	2018	2017
Net income	$ 1,799	$ 3,935	$ 1,318	$ 1,341
Other comprehensive (loss) income:				
Foreign currency translation adjustments	(269)	661	58	274
Other comprehensive (loss) income	(269)	661	58	274
Comprehensive income	$ 1,530	$ 4,596	$ 1,376	$ 1,615

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

Table of Contents

Wayside Technology Group, Inc. and Subsidiaries

Condensed Consolidated Statement of Stockholders' Equity

(Unaudited)

(Amounts in thousands, except share amounts)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Treasury Shares	Treasury Amount	Retained Earnings	Accumulated Other Comprehensive (loss)	Total
Balance at January 1, 2018	5,284,500	$ 53	$ 31,257	829,671	$ (14,207)	$ 22,522	$ (913)	$ 38,712
Net income	—	—	—	—	—	1,799	—	1,799
Translation adjustment	—	—	—	—	—	—	(269)	(269)
Dividends paid	—	—	—	—	—	(2,301)	—	(2,301)
Share-based compensation expense	—	—	2,618	—	—	—	—	2,618
Restricted stock grants (net of forfeitures) and adjustments	—	—	(1,634)	(115,824)	1,799	—	—	165
Treasury shares repurchased	—	—	—	72,430	(1,018)	—	—	(1,018)
Balance at September 30, 2018	5,284,500	$ 53	$ 32,241	786,277	$ (13,426)	$ 22,020	$ (1,182)	$ 39,706

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

Wayside Technology Group, Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(Amounts in thousands)

	Nine months ended September 30,	
	2018	2017
Cash flows from operating activities		
Net income	$ 1,799	$ 3,935
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization expense	358	359
(Benefit) for doubtful accounts receivable	—	(95)
Deferred income tax expense	7	181
Share-based compensation expense	2,618	1,026
Loss on disposal of fixed assets	22	—
Changes in operating assets and liabilities:		
Accounts receivable	(4,147)	21,101
Inventory	1,029	(69)
Prepaid expenses and other current assets	24	169
Vendor prepayments	2,867	(7,471)
Accounts payable and accrued expenses	163	(25,405)
Other assets and liabilities	(109)	(96)
Net cash provided by (used in) operating activities	4,631	(6,365)
Cash flows used in investing activities		
Purchase of equipment and leasehold improvements	(243)	(339)
Net cash used in investing activities	(243)	(339)
Cash flows used in financing activities		
Purchase of treasury stock	(1,018)	(2,841)
Borrowings under revolving credit facility	10,000	2,000
Repayments of borrowings under revolving credit facility	(10,000)	—
Dividends paid	(2,301)	(2,298)
Net cash used in financing activities	(3,319)	(3,139)
Effect of foreign exchange rate on cash	(135)	384
Net increase (decrease) in cash and cash equivalents	934	(9,459)
Cash and cash equivalents at beginning of period	5,530	13,524
Cash and cash equivalents at end of period	$ 6,464	$ 4,065

Supplementary disclosure of cash flow information:		
Income taxes paid	$ 1,779	$ 1,944

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

Table of Contents

Wayside Technology Group, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements

September 30, 2018

(Unaudited)

(Amounts in tables in thousands, except share and per share amounts)

1. Basis of Presentation:

The accompanying unaudited condensed consolidated financial statements of Wayside Technology Group, Inc. and its subsidiaries (collectively, the "Company"), have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, the financial statements do not include all of the information and footnotes required by U.S. GAAP for complete audited financial statements.

The preparation of these condensed consolidated financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to product returns, bad debts, inventories, intangible assets, income taxes, stock-based compensation, evaluation of performance obligations and allocation of revenue to distinct items, contingencies and litigation. The Company bases its estimates on its historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. In the opinion of the Company's management, all adjustments that are of a normal recurring nature, considered necessary for fair presentation, have been included in the accompanying condensed consolidated financial statements. The Company's actual results may differ from these estimates under different assumptions or conditions. The unaudited condensed consolidated statements of income for the interim periods are not necessarily indicative of results for the full year. For further information, refer to the consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K filed with the Securities Exchange Commission for the year ended December 31, 2017.

Effective January 1, 2018 we adopted the requirements of Accounting Standards Update, or ASU, No. 2014-09 Revenue from Contracts with customers, or Accounting Standard Codification ("ASC") 606 using the full retrospective method, as discussed in detail in Note 5. All amounts and disclosures set forth in this Quarterly Report on Form 10-Q have been updated to comply with ASC 606 as discussed in Note 5.

Reclassifications

Certain reclassifications and immaterial revisions have been made to the prior period financial statements to conform to the current-year presentation.

2. Recently issued accounting standards:

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU 2014-09, Revenue from Contracts with Customers, superseding the previous revenue recognition requirements, along with most existing industry-specific guidance. In March, April, May and December 2016, the FASB issued additional updates to the new accounting standard which provide supplemental adoption guidance and clarifications. The guidance requires an entity to review contracts in five steps: 1) identify the contract, 2) identify performance obligations, 3) determine the transaction price, 4) allocate the transaction price, and 5) recognize revenue in order to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new standard also requires enhanced disclosures regarding the nature, amount, timing and uncertainty of revenue arising from contracts with customers. The Company adopted the new standard on January 1, 2018, using the full retrospective method which required us to restate our historical financial information to reflect the adoption as of the earliest reporting period presented. The most significant impact of adopting the standard relates to the determination of whether the Company is acting as a principal or an agent in the sale of third party security software and software that is highly interdependent with support, as well as maintenance, support or other services. See Footnote 5 (Revenue Recognition).

Table of Contents

In February 2016, the FASB issued ASU 2016-02, Leases ("ASU 2016-02"). ASU 2016-02 supersedes the lease guidance under FASB ASC Topic 840, Leases, resulting in the creation of FASB ASC Topic 842, Leases. ASU 2016-02 requires a lessee to recognize in the statement of financial position a liability to make lease payments and a right-of-use asset representing its right to use the underlying asset for the lease term. Leases will be classified as either finance or operating leases with classification affecting the pattern of expense recognition in the statement of earnings. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2018. Early adoption is permitted. The Company is currently assessing the potential impact of adopting ASU 2016-02 on its consolidated financial statements. It is expected that assets and liabilities will increase as a result of the adoption of this standard.

In June 2016, the FASB issued Accounting Standards Update No. 2016-13, Financial Instruments - Credit Losses (Topic 326) ("ASU No. 2016-13"). ASU No. 2016-13 revises the methodology for measuring credit losses on financial instruments and the timing of when such losses are recorded. ASU No. 2016-13 is effective for the Company in the first quarter of 2020, with early adoption permitted, and is to be applied using a modified retrospective approach. The Company is currently evaluating the potential effects of adopting the provisions of ASU No. 2016-13 on its consolidated financial statements, particularly its recognition of allowances for accounts receivable.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (“ASU 2016-15”) which reduces diversity in practice in how certain transactions are classified in the statement of cash flows. The new standard is effective for the Company beginning with the first quarter of 2018. The adoption of this guidance did not have a material impact on the Company’s consolidated financial statements.

In October 2016, the FASB issued ASU 2016-16, “Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory.” This amendment is intended to improve accounting for the income tax consequences of intra-entity transfers of assets other than inventory. In accordance with this guidance, an entity should recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. The ASU is effective for the Company beginning in fiscal 2019. Early adoption is permitted in fiscal 2018 with modified retrospective application. The Company is continuing to evaluate the impact of the adoption of this guidance on its consolidated financial statements.

In May 2017, the FASB issued ASU No. 2017-09, “Scope of Modification Accounting”, to reduce diversity in practice and provide clarity regarding existing guidance in ASC 718, “Stock Compensation”. The amendments in this updated guidance clarify that an entity should apply modification accounting in response to a change in the terms and conditions of an entity’s share-based payment awards unless three newly specified criteria are met. This guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within that reporting period. The new guidance was effective for the Company on a prospective basis beginning on January 1, 2018 and did not impact the Company’s Consolidated Financial Statements as it is not the Company’s practice to change either the terms or conditions of stock-based payment awards once they are granted.

In August 2017, the FASB issued ASU No. 2017-12, Derivatives and Hedging (Topic 815) – Targeted Improvements to Accounting for Hedging Activities, which improves the financial reporting of hedging relationships to better portray the economic results of an entity’s risk management activities in its financial statements. The amendments in this update also make certain targeted improvements to simplify the application of the hedge accounting guidance in current U.S. GAAP. ASU No. 2017-12 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years; the ASU allows for early adoption in any interim period after issuance of the update. The Company is currently assessing the impact this ASU will have on its consolidated financial statements.

In February 2018, the FASB issued ASU 2018-02, “Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income” (“ASU 2018-02”), which permits the reclassification of stranded tax effects resulting from the Tax Cuts and Jobs Act (the “TCJA” or “U.S. tax reform”) from Accumulated other comprehensive income (loss) to Retained earnings. This new guidance is effective for the Company beginning on January 1, 2019 with early adoption permitted and must be applied either in the period of adoption or retrospectively to periods in which the effects of the TCJA are recognized. The Company is continuing to evaluate the impact of the adoption of this guidance on its consolidated financial statements.

In March 2018, the FASB issued ASU 2018-05, “Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118 (SEC Update), Income Taxes (Topic 740)”. ASU 2018-05 provides guidance regarding the recording of tax impacts where uncertainty exists, in the period of adoption of the 2017 U.S. Tax Cuts and Jobs Act (the “2017 Tax Act”), which allowed companies to reflect provisional amounts for those specific income tax effects of the 2017 Tax Act for which the accounting under ASC Topic 740 is incomplete but for which a reasonable estimate could be

Table of Contents

determined. The Company completed its Federal and State income tax filings for 2017 with no material change to amounts previously reported.

In June 2018, the FASB issued Accounting Standards Update ("ASU") No. 2018-07, "Compensation — Stock Compensation (Topic 718), Improvements to Nonemployee Share-Based Payment Accounting," which aligns the measurement and classification guidance for share-based payments to nonemployees with that for employees, with certain exceptions. It expands the scope of ASC 718 to include share-based payments granted to nonemployees in exchange for goods or services used or consumed in the entity's own operations and supersedes the guidance in ASC 505-50. The ASU retains the existing cost attribution guidance, which requires entities to recognize compensation cost for nonemployee awards in the same period and in the same manner (i.e., capitalize or expense) they would if they paid cash for the goods or services, but it moves the guidance to ASC 718. The guidance also allows nonpublic entities to account for nonemployee awards using certain practical expedients that are already available for employee awards, but the same accounting policies must be used for awards to both employees and nonemployees. ASU 2018-07 is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently evaluating the impact of adopting this guidance.

In July 2018, the FASB issued ASU 2018-09 – Codification Improvements, which facilitates amendments to a variety of topics to clarify, correct errors in, or make minor improvements to the accounting standards codification. The effective date of the standard is dependent on the facts and circumstances of each amendment. Some amendments do not require transition guidance and will be effective upon the issuance of this standard. A majority of the amendments in ASU 2018-09 will be effective in annual periods beginning after December 15, 2018. We will be required to adopt this standard in the first quarter of fiscal 2019. This standard is not expected to have a material impact on our consolidated financial statements and related disclosures.

3. Foreign Currency Translation:

Assets and liabilities of the Company's foreign subsidiaries have been translated using the end of the reporting period exchange rates, and related revenues and expenses have been translated at average rates of exchange in effect during the period. Foreign currency transaction gains and losses are recorded as income or expenses as amounts are settled. The net sales from our foreign operations for the first nine months of 2018 were $13.9 million as compared to $14.1 million in the first nine months of 2017. The net sales from our foreign operations for the third quarter of 2018 were $4.0 million as compared to $4.6 million in the third quarter of 2017.

4. Comprehensive Income:

Cumulative translation adjustments have been classified within accumulated other comprehensive loss, which is a separate component of stockholders' equity in accordance with FASB ASC Topic 220, "Comprehensive Income."

5. Revenue Recognition:

Effective January 1, 2018, we adopted ASC 606 using the full retrospective method, which requires us to restate our historical financial information to reflect the adoption as of the earliest reporting period presented. There was no adjustment to equity as a result of the adoption. The most significant impact of adopting the standard relates to the determination of whether the Company is acting as a principal or an agent in the sale of third party security software and software that is highly interdependent with support, as well as maintenance, support and other services. Historically, under the transfer of risk and rewards model of revenue recognition, the Company has accounted for primarily all of its sales on a gross basis. The new guidance requires the Company to identify performance obligations and assess transfer of control. While assessing its performance obligations for sales of security software and software subscriptions that are highly interdependent with support, the Company determined that the vendor has ongoing performance obligations with the end customer that are not separately identifiable from the software itself. The Company also determined that the vendor has ongoing performance obligation for sales of certain third-party maintenance, support and service contracts. In these instances, the Company has determined that it does not have control and is acting as an agent in the sale. When acting as an agent in a transaction, the Company accounts for sales on a net basis, with the vendor cost associated with the sale recognized as a reduction of revenue.

Table of Contents

ASC 606 Adoption Impact to Previously Reported Results

The tables below present historical information adjusted as if the standard had been adopted on January 1, 2017 for all periods presented.

	Nine months ended September 30, 2017			Three months ended September 30, 2017		
	As Reported	Impact of Adoption	As Adjusted	As Reported	Impact of Adoption	As Adjusted
Total						
Net sales	$ 322,423	$ (206,293)	$ 116,130	$ 106,646	$ (67,628)	$ 39,018
Cost of sales	302,848	(206,293)	96,555	100,403	(67,628)	32,775
Gross profit	$ 19,575	$ —	$ 19,575	$ 6,243	$ —	$ 6,243

	Nine months ended September 30, 2017			Three months ended September 30, 2017		
	As Reported	Impact of Adoption	As Adjusted	As Reported	Impact of Adoption	As Adjusted
Lifeboat Distribution Segment:						
Net sales	$ 300,344	$ (196,459)	$ 103,885	$ 100,188	$ (65,479)	$ 34,709
Cost of sales	283,471	(196,459)	87,012	94,771	(65,479)	29,292
Gross profit	$ 16,873	$ —	$ 16,873	$ 5,417	$ —	$ 5,417
TechXtend Segment:						
Net sales	$ 22,079	$ (9,834)	$ 12,245	$ 6,458	$ (2,149)	$ 4,309
Cost of sales	19,377	(9,834)	9,543	5,632	(2,149)	3,483
Gross profit	$ 2,702	$ —	$ 2,702	$ 826	$ —	$ 826

The core principle of ASC 606 is to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration the entity expects to be entitled in exchange for those goods or services. This principle is achieved through applying the following five-step approach:

Identification of the contract, or contracts, with a customer — A contract with a customer exists when (i) we enter into an enforceable contract with a customer that defines each party's rights regarding the goods or services to be transferred and identifies the payment terms related to these goods or services, (ii) the contract has commercial substance and, (iii) we determine that collection of substantially all consideration for goods or services that are transferred is probable based on the customer's intent and ability to pay the promised consideration. We apply judgment in determining the customer's ability and intention to pay, which is based on a variety of factors including the customer's historical payment experience or, in the case of a new customer, published credit and financial information pertaining to the customer. The Company considers customer purchase orders, which in some cases are governed by master agreements or general terms and conditions of sale, to be contracts with customers. All revenue is generated from contracts with customers.

Identification of the performance obligations in the contract — Performance obligations promised in a contract are identified based on the goods or services that will be transferred to the customer that are capable of being distinct, whereby the customer can benefit from the goods or service either on its own or together with other resources that are readily available from third parties or from us, and are distinct in the context of the contract, whereby the transfer of the goods or services is separately identifiable from other promises in the contract. To the extent a contract includes multiple promised goods or services, we apply judgment to determine whether promised goods or services are capable of being distinct in the context of the contract. If these criteria are not met the promised goods or services are accounted for as a combined performance obligation.

Table of Contents

Determination of the transaction price —The transaction price is determined based on the consideration to which we will be entitled in exchange for transferring goods or services to the customer. Net sales are recorded net of estimated discounts, rebates, and returns. Vendor rebates and price protection are recorded when earned as a reduction to cost of sales or merchandise inventory, as applicable. Cooperative reimbursements from vendors, which are earned and available, are recorded in the period the related advertising expenditure is incurred. Cooperative reimbursements are recorded as a reduction of cost of sales.

Allocation of the transaction price to the performance obligations in the contract — If the contract contains a single performance obligation, the entire transaction price is allocated to the single performance obligation. Contracts that contain multiple performance obligations require an allocation of the transaction price to each performance obligation based on a relative standalone selling price, or SSP, basis. We determine standalone SSP based on the price at which the performance obligation is sold separately. If the standalone selling price is not observable through established standard prices, we use judgement and estimate the standalone selling price taking into account available information such as market pricing and pricing related to similar products. Contracts with a significant financing component are discounted to their present value at contract inception and accreted up to the expected payment amounts. These contracts generally offer customers extended payment terms of up to three years.

Recognition of revenue when, or as, we satisfy a performance obligation — The Company recognizes revenue when its performance obligations are complete, and control of the specified goods or services pass to the customer. The Company considers the following indicators in determining when control passes to the customer: (i) the Company has a right to payment for the product or service (ii) the customer has legal title to the product, (iii) the Company has transferred physical possession of the product (iv) the Customer has the significant risk and rewards of ownership of the product and (v) the customer has accepted the product. Substantially all our performance obligations are satisfied at a point in time, as our obligation is to deliver a product or fulfill an order for a third party to deliver ongoing services, maintenance or support.

Disaggregation of Revenue

We generate revenue from the re-sale of third party software licenses, subscriptions, hardware, and related service contracts. Finance fees related to sales are classified as interest income. The following table depicts the disaggregation of revenue according to revenue type and is consistent with how we evaluate our financial performance:

Net sales	(Unaudited) Nine months ended		(Unaudited) Three months ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Hardware and software product	$ 120,073	$ 104,417	$ 44,100	$ 35,556
Software - security & highly interdependent with support	5,029	4,357	1,433	1,343
Maintenance, support & other services	7,287	7,356	2,390	2,119
Net sales	$ 132,389	$ 116,130	$ 47,923	$ 39,018

Hardware and software product - Hardware product consists of sales of hardware manufactured by third parties. Hardware product is delivered from our warehouse or drop shipped directly from the vendor. Revenue from our hardware products is recognized on a gross basis, with the selling price to the customer as net sales, and the cost of the related product as cost of sales, upon transfer of control to the customer, as the Company is acting a principal in the transaction. Control is generally deemed to have passed to the customer upon transfer of title and risk of ownership.

Software product consists of sales of perpetual and term software licenses for products developed by third party vendors, which are distinct from related maintenance and support. Software licenses are delivered via electronic license keys provided by the vendor to the end user. Revenue from the sale of software products is recognized on a gross basis, with the selling price to the customer as net sales, and the cost of the related product as cost of sales, upon transfer of control to our customers as the Company is a principal in the transaction. Control is deemed to have passed to the customer when they acquire the right to use or copy the software under license as substantially all product functionality is available to the customer at the time of sale.

Software maintenance and support, commonly known as software assurance or post contract support, consists of software updates and technical support provided by the software vendor to the licensor over a period of time. In cases where the software maintenance is distinct from the related software license, software maintenance is accounted for as a separate performance obligation. In cases where the software maintenance is not distinct from the related software license, it is accounted for as a single performance obligation with the related license. We utilize judgement in determining whether the maintenance is distinct from the software itself. This involves considering if the software provides its original intended functionality without the updates, or is dependent on frequent, or continuous updates to maintain its functionality. See Allocation of the transaction price to the performance obligations in the contract for a discussion of the allocation of maintenance and support costs when they are distinct from the related software licenses and Software - security and highly interdependent with support for a discussion of maintenance and support costs when they are not distinct from the related software license.

Software - security and highly interdependent with support - Software - security software and software highly interdependent with support consists of sales of security subscriptions and other licensed software products whose functionality is highly interdependent with, and therefore not distinct from, related software maintenance. Delivery of the software license and related support over time is considered a single performance obligation of the third-party vendor for these products. The Company is an agent in these transactions, with revenue being recorded on a net basis when its performance obligation of processing a valid order between the supplier and customer contracting for the services is complete.

Maintenance, support and other services revenue - Maintenance, support and other services revenue consists of third-party post-contract support that is not critical or essential to the core functionality of the related licensed software, and, to a lesser extent, from third-party professional services, software as a service, and cloud subscriptions. Revenue from maintenance, support and other service revenues is recognized on a net basis, upon fulfillment of an order to the customer, as the Company is an agent in the transaction, and its performance obligations are complete at the time a valid order between the parties is processed.

Costs to obtain and fulfill a contract - We pay commissions and related payroll taxes to sales personnel when customers are invoiced. These costs are recorded as selling general and administrative expenses in the period earned as all of our performance obligations are complete within a short window of processing the order.

Contract balances -Accounts receivable is recorded at the invoiced amount, net of an allowance for doubtful accounts and returns. A receivable is recognized in the period we deliver goods or provide services or when our right to consideration is unconditional. Payment terms on invoiced amounts are typically 30-75 days. The balance of accounts receivable, net of allowance for doubtful accounts and returns, as of December 31, 2017 and September 30, 2018 is presented in the accompanying condensed consolidated balance sheets. Accounts receivable-long-term result from product sales with extended payment terms that are discounted to their present values at the Company’s estimates of prevailing market rates at the time of the sale. The Company has determined that these amounts do not represent variable consideration as the amount earned is fixed. In subsequent periods, the accounts receivable is increased to the amounts due and payable by the customers through the accretion of interest income on the unpaid accounts receivable due in future years. The amounts due under these long-term accounts receivable due within one year are reclassified to the current portion of accounts receivable and are shown net of reserves. As our revenues are generally recognized at a point in time in the same period as they are billed, we have no deferred revenue balances. Provisions for doubtful accounts including long-term accounts receivable and returns are estimated based on historical write offs, sales returns and credit memo analysis which are adjusted to actual on a periodic basis.

Principal versus agent considerations – The Company determines whether it is acting as a principal or agent in a transaction by assessing whether it controls a good or service prior to it being transferred to a customer, with control being defined as having the ability to direct the use of and obtain the benefits from the asset. The Company considers the following indicators, among others, in making the determination: 1) the Company is primarily responsible for fulfilling the promise to provide the promised good or service, 2) the Company has inventory risk, before or after the specified good or service has been transferred to the customer, 3) the Company has discretion in establishing price for the specified good or service. Generally, we conclude that we are a principal in transactions where software or hardware products containing their core functionality are delivered to the customer at the time of sale and are agents in transactions where we are arranging for the provision of future performance obligations by a third party. As we enter into distribution agreements with third-party service providers, we evaluate whether we are acting as a principal or agent for each product sold under the agreement based on the nature of the product or service, and our performance obligations. Products for which there are significant ongoing third-party performance obligations include software maintenance, which includes periodic software updates and support, security software that is highly interdependent with maintenance, software as a service, cloud and third party professional services. Sales of hardware and software products where we are a principal are recorded on a gross

Table of Contents

basis with the selling price to the customer recorded as sales and the cost of the product or software recorded as cost of sales. Sales where we are acting as an agent are recognized on a net basis at the date our performance obligations are complete. Under net revenue recognition, the cost paid to the vendor or third-party service provider is recorded as a reduction to sales, resulting in revenue being equal to the gross profit on the transaction.

6. Fair Value:

The carrying amounts of financial instruments, including cash and cash equivalents, short-term accounts receivable and accounts payable approximated fair value at September 30, 2018 and December 31, 2017 because of the relative short maturity of these instruments. The Company's accounts receivable long-term is discounted to their present value at estimated prevailing market rates at the date of sale which approximates current rates.

7. Balance Sheet Detail:

Accounts Receivable – From time to time, we sell accounts receivable to a financial institution on a non-recourse basis. The financial institution is responsible for all servicing of the receivables purchased. At September 30, 2018, accounts receivable includes $6.5 million of accounts receivable which have been sold to a financial institution with payment due to the Company on November 12, 2018. The receivables are recorded at their discounted fair value at September 30 ,2018.

Equipment and leasehold improvements consist of the following:

September 30, (Unaudited)	December 31,