

## Section 1: 10-Q (FORM 10-Q)

[Table of Contents](#)

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**FORM 10-Q**

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

For the quarterly period ended April 30, 2012

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: 001-35198

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**Pandora Media, Inc.**

(Exact name of registrant as specified in its charter)

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Delaware  
(State or other jurisdiction of  
incorporation or organization)

94-3352630  
(I.R.S. Employer  
Identification No.)

2101 Webster Street, Suite 1650  
Oakland, CA  
(Address of principal executive offices)

94612  
(Zip Code)

(510) 451-4100  
(Registrant's telephone number, including area code)

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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 to 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, 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  (Do not check if a smaller reporting company) 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 of registrant's common stock outstanding as of May 25, 2012 was: 166,654,653



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**Table of Contents**

**Pandora Media, Inc.**  
**FORM 10-Q Quarterly Report**  
**Table of Contents**

	<b><u>Page No.</u></b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
Item 1.	3
<u>Financial Statements</u>	
<u>Condensed Consolidated Balance Sheets as of January 31, 2012 and April 30, 2012 (unaudited)</u>	3
<u>Condensed Consolidated Statements of Operations for the Three Months Ended April 30, 2011 and 2012 (unaudited)</u>	4
<u>Condensed Consolidated Statements of Comprehensive Loss for the Three Months Ended April 30, 2011 and 2012 (unaudited)</u>	5
<u>Condensed Consolidated Statements of Cash Flows for the Three Months Ended April 30, 2011 and 2012 (unaudited)</u>	6
<u>Notes to Condensed Consolidated Financial Statements (unaudited)</u>	7
Item 2.	19
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	
Item 3.	27
<u>Quantitative and Qualitative Disclosures About Market Risk</u>	
Item 4.	27
<u>Controls and Procedures</u>	
<b><u>PART II. OTHER INFORMATION</u></b>	
Item 1.	27
<u>Legal Proceedings</u>	
Item 1A.	28
<u>Risk Factors</u>	
Item 2.	28
<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	
Item 6.	28
<u>Exhibits</u>	
<u>Signatures</u>	30

## [Table of Contents](#)

### PART I. FINANCIAL INFORMATION

#### Item 1. Financial Statements

**Pandora Media, Inc.**  
**Condensed Consolidated Balance Sheets**  
**(In thousands, except share and per share amounts)**  
**(Unaudited)**

	As of January 31, 2012	As of April 30, 2012
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 44,126	\$ 44,690
Short-term investments	46,455	35,900
Accounts receivable, net of allowances of \$590 and \$448 at January 31 and April 30, 2012, respectively	66,738	70,531
Prepaid expenses and other current assets	2,806	3,247
Total current assets	160,125	154,368
Property and equipment, net	15,576	15,246
Other assets	2,314	2,247
Total assets	<u>\$ 178,015</u>	<u>\$ 171,861</u>
<b>Liabilities and stockholders' equity</b>		
Current liabilities:		
Accounts payable	\$ 2,053	\$ 1,595
Accrued liabilities	3,838	5,642
Accrued royalties	33,822	38,136
Deferred revenue	19,232	21,741
Accrued compensation	11,962	9,517
Total current liabilities	70,907	76,631
Other long-term liabilities	2,568	3,380
Total liabilities	<u>73,475</u>	<u>80,011</u>
<b>Stockholders' equity:</b>		
Preferred stock, \$0.0001 par value; 10,000,000 shares authorized as of January 31 and April 30, 2012, respectively; no shares issued and outstanding as of January 31 and April 30, 2012	—	—
Common stock, \$0.0001 par value; 1,000,000,000 shares authorized as of January 31 and April 30, 2012, respectively; 163,569,361 and 166,465,483 shares issued and outstanding as of January 31 and April 30, 2012, respectively	16	17
Additional paid-in capital	205,955	213,489
Accumulated deficit	(101,426)	(121,654)
Accumulated other comprehensive loss	(5)	(2)
Total stockholders' equity	<u>104,540</u>	<u>91,850</u>
Total liabilities and stockholders' equity	<u>\$ 178,015</u>	<u>\$ 171,861</u>

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

[Table of Contents](#)

**Pandora Media, Inc.**  
**Condensed Consolidated Statements of Operations**  
**(In thousands, except per share amounts)**  
**(Unaudited)**

	<b>Three Months Ended</b>	
	<b>April 30,</b>	
	<b>2011</b>	<b>2012</b>
Revenue:		
Advertising	\$43,661	\$ 70,597
Subscription services and other	7,379	10,187
Total revenue	51,040	80,784
Costs and expenses:		
Cost of revenue	4,360	6,917
Product development	2,731	4,119
Marketing and sales	12,964	23,460
General and administrative	6,943	10,612
Content acquisition	29,158	55,818
Total costs and expenses	56,156	100,926
Loss from operations	(5,116)	(20,142)
Other income (expense):		
Interest income	2	32
Interest expense	(109)	(124)
Other income (expense), net	(1,509)	—
Loss before provision for income taxes	(6,732)	(20,234)
Provision for income taxes	(22)	6
Net loss	(6,754)	(20,228)
Accretion of redeemable convertible preferred stock	(70)	—
Increase in cumulative dividends payable upon conversion or liquidation of redeemable convertible preferred stock	(2,320)	—
Net loss attributable to common stockholders	<u>\$ (9,144)</u>	<u>\$ (20,228)</u>
Basic and diluted net loss per share attributable to common stockholders	<u>\$ (0.61)</u>	<u>\$ (0.12)</u>
Weighted-average number of shares used in computing basic per share amounts	<u>14,900</u>	<u>165,404</u>

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

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[Table of Contents](#)

**Pandora Media, Inc.**  
**Condensed Consolidated Statements of Comprehensive Loss**  
**(In thousands, except per share amounts)**  
**(Unaudited)**

	<b>Three Months Ended</b>	
	<b>April 30,</b>	
	<b>2011</b>	<b>2012</b>
Net loss	\$(6,754)	(20,228)
Other comprehensive loss:		
Unrealized gains on marketable securities, net	—	3
Other comprehensive loss:	\$(6,754)	(20,225)
Total comprehensive loss	<u>\$(6,754)</u>	<u>\$(20,225)</u>

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

[Table of Contents](#)

**Pandora Media, Inc.**  
**Condensed Consolidated Statements of Cash Flows**  
**(In thousands)**  
**(Unaudited)**

	Three Months Ended	
	April 30,	
	2011	2012
<b>Operating Activities</b>		
Net loss	\$(6,754)	\$(20,228)
Adjustments to reconcile net loss to net cash provided (used in) by operating activities:		
Depreciation and amortization	759	1,541
(Gain) loss on disposition of assets	—	32
Stock-based compensation	936	5,500
Remeasurement of preferred stock warrants	1,523	—
Amortization of premium on investments	—	92
Amortization of debt issuance cost and debt discount	1	66
Changes in assets and liabilities:		
Accounts receivable	1,007	(3,793)
Prepaid expenses and other assets	(1,406)	(433)
Accounts payable and accrued liabilities	(624)	1,022
Accrued royalties	3,006	4,314
Accrued compensation	2,781	(2,445)
Deferred revenue	1,546	2,509
Reimbursement of cost of leasehold improvements	—	1,243
Net cash provided (used in) by operating activities	<u>2,775</u>	<u>(10,580)</u>
<b>Investing Activities</b>		
Purchases of property and equipment	(2,086)	(1,243)
Purchase of short-term investments	—	(17,641)
Maturities of short-term investments	—	28,100
Net cash provided by (used) in investing activities	<u>(2,086)</u>	<u>9,216</u>
<b>Financing Activities</b>		
Repayments of debt	(164)	—
Proceeds from issuance of common stock	145	1,928
Net cash provided by (used in) financing activities	<u>(19)</u>	<u>1,928</u>
Net increase in cash and cash equivalents	670	564
Cash and cash equivalents at beginning of period	43,048	44,126
Cash and cash equivalents at end of period	<u>\$43,718</u>	<u>\$ 44,690</u>

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

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements**

**1. Description of Business and Basis of Presentation**

Pandora Media, Inc. (the “Company” or “Pandora”) provides an internet radio service in the United States, offering a personalized experience for each of its listeners. The Company has developed a form of radio that uses intrinsic qualities of music to initially create stations that then adapt playlists in real-time based on the individual feedback of each listener.

The Company was incorporated as a California corporation in January 2000 and reincorporated as a Delaware corporation in December 2010.

***Basis of Presentation***

The interim unaudited condensed consolidated financial statements and accompanying notes have been prepared in accordance with United States generally accepted accounting principles (“U.S. GAAP”) and include the accounts of the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation. In the opinion of the Company’s management, the interim unaudited condensed consolidated financial statements include all adjustments, which include only normal recurring adjustments, necessary for the fair presentation of the Company’s financial position for the periods presented. These interim unaudited condensed consolidated financial statements are not necessarily indicative of the results expected for the full fiscal year or for any subsequent period and should be read in conjunction with the audited consolidated financial statements and related notes included in the Company’s Annual Report on Form 10-K for the fiscal year ended January 31, 2012.

***Use of Estimates***

The preparation of financial statements in conformity with U.S. GAAP requires management to make certain estimates, judgments, and assumptions that affect the reported amounts of assets and liabilities and the related disclosures at the date of the financial statements, as well as the reported amounts of revenue and expenses during the periods presented. Estimates are used for determining selling prices for elements sold in multiple-element arrangements, the allowance for doubtful accounts, the fair value of common stock through the date of the Company’s initial public offering (“IPO”) in June 2011, stock-based compensation, fair values of investments, income taxes, and accrued royalties. To the extent there are material differences between these estimates, judgments, or assumptions and actual results, the Company’s financial statements could be affected. In many cases, the accounting treatment of a particular transaction is specifically dictated by U.S. GAAP and does not require management’s judgment in its application. There are also areas in which management’s judgment in selecting among available alternatives would not produce a materially different result.

***Fiscal Year***

All references herein to a fiscal year refer to the 12 months ended January 31 of such year, and references to the first, second, third and fourth fiscal quarters refer to the three months ended April 30, July 31, October 31 and January 31, respectively.



**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

**2. Summary of Significant Accounting Policies**

There have been no material changes to the Company's significant accounting policies as compared to those described in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2012.

***Concentration of Credit Risk***

For the three months ended April 30, 2011 the Company had one customer that accounted for 12% of total revenue. For the three months ended April 30, 2012, the Company had no customers that accounted for more than 10% of the Company's total revenue.

As of January 31 and April 30, 2012, the Company had no customers that accounted for more than 10% of the Company's total accounts receivable.

***Recently Issued Accounting Standards***

Effective February 1, 2012, the Company adopted Accounting Standards Update ("ASU") No. 2011-04, "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards ("IFRS')." The ASU updates the accounting guidance to clarify and align Fair Value Measurement within U.S. GAAP and International Financial Reporting Standards. In addition, the ASU updates certain requirements for measuring fair value and for disclosure around fair value measurement. It does not require additional fair value measurements and the ASU was not intended to establish valuation standards or affect valuation practices outside of financial reporting. The adoption of ASU 2011-04 did not have a significant impact on the Company's consolidated financial position or results of operations.

Effective February 1, 2012, the Company adopted ASU No. 2011-05, "Presentation of Comprehensive Income." The adoption of ASU 2011-05 concerns presentation and disclosure only and did not have an impact on the Company's consolidated balance sheets or results of operations. ASU 2011-05 requires retrospective application and separate consolidated statements of comprehensive income are included in these financial statements.

Effective February 1, 2012, the Company adopted ASU No. 2011-12, "Deferral of the Effective Date for Amendments to the Presentation of Reclassification of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05." The adoption of ASU 2011-12 concerns presentation and disclosure only and did not have an impact on the Company's consolidated financial position or results of operations.

[Table of Contents](#)

Pandora Media, Inc.

Notes to Condensed Consolidated Financial Statements - Continued

3. Composition of Certain Financial Statement Captions

Cash, Cash Equivalents and Short-term Investments

Cash, cash equivalents and short-term investments consisted of the following:

	As of January 31, 2012	As of April 30, 2012
(in thousands)		
Cash and cash equivalents:		
Cash	\$ 6,604	\$ 5,411
Money market funds	31,614	34,780
Commercial paper	2,893	4,499
Corporate debt securities	3,015	—
Total cash and cash equivalents	<u>\$ 44,126</u>	<u>\$44,690</u>
Short-term investments:		
Commercial paper	\$ 27,587	\$23,789
Corporate debt securities	17,968	9,607
U.S. agency notes	900	2,504
Total short-term investments	<u>\$ 46,455</u>	<u>\$35,900</u>
Cash, cash equivalents and short-term investments	<u>\$ 90,581</u>	<u>\$80,590</u>

The Company's short-term investments have maturities of less than 12 months and are classified as available for sale. As of January 31 and April 30, 2012 the cost basis of the Company's cash and cash equivalents approximated their fair values and as a result, no unrealized gains or losses were recorded as of January 31 and April 30, 2012.

The following tables summarize the Company's available-for-sale securities' adjusted cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category as of January 31 and April 30, 2012 (in thousands).

	As of January 31, 2012			
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
Money market funds	\$31,614	\$ —	\$ —	\$31,614
Commercial paper	30,481	—	(1)	30,480
Corporate debt securities	20,987	1	(5)	20,983
U.S. agency notes	900	—	—	900
Total cash equivalents and marketable securities	<u>\$83,982</u>	<u>\$ 1</u>	<u>\$ (6)</u>	<u>\$83,977</u>

	As of April 30, 2012			
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
Money market funds	\$34,780	\$ —	\$ —	\$34,780
Commercial paper	28,288	1	(1)	28,288
Corporate debt securities	9,609	—	(2)	9,607
U.S. agency notes	2,504	—	—	2,504
Total cash equivalents and marketable securities	<u>\$75,181</u>	<u>\$ 1</u>	<u>\$ (3)</u>	<u>\$75,179</u>

The Company's investment policy requires investments to be investment grade, primarily rated "A1" by Standard & Poor's or "P1" by Moody's or better for short-term investments, with the objective of minimizing the potential risk of principal loss. In addition, the investment policy limits the amount of credit exposure to any one issuer.

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

The unrealized losses on the Company's available-for-sale securities were primarily a result of unfavorable changes in interest rates subsequent to the initial purchase of these securities. As of April 30, 2012, the Company owned 12 securities that were in an unrealized loss position. The Company does not intend nor expect to need to sell these securities before recovering the associated unrealized losses. It expects to recover the full carrying value of these securities. As a result, no portion of the unrealized losses at April 30, 2012 is deemed to be other-than-temporary and the unrealized losses are not deemed to be credit losses. No available-for-sale securities have been in an unrealized loss position for 12 months or more. When evaluating the investments for other-than-temporary impairment, the Company reviews factors such as the length of time and extent to which fair value has been below cost basis, the financial condition of the issuer and any changes thereto, and the Company's intent to sell, or whether it is more likely than not it will be required to sell, the investment before recovery of the investment's amortized cost basis. During the three months ended April 30, 2012, the Company did not recognize any impairment charges.

## [Table of Contents](#)

### Pandora Media, Inc.

#### Notes to Condensed Consolidated Financial Statements - Continued

#### 4. Fair Value

The Company records cash equivalents and short-term investments at fair value.

Fair value is an exit price, representing the amount that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. Fair value measurements are required to be disclosed by level within the following fair value hierarchy:

Level 1 – Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date.

Level 2 – Inputs (other than quoted prices included in Level 1) are either directly or indirectly observable for the asset or liability through correlation with market data at the measurement date and for the duration of the instrument's anticipated life.

Level 3 – Inputs lack observable market data to corroborate management's estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model. As of January 31 and April 30, 2012 the Company did not hold any Level 3 assets.

When determining fair value, whenever possible the Company uses observable market data, and relies on unobservable inputs only when observable market data is not available.

The fair value of these financial assets and liabilities was determined using the following inputs at January 31 and April 30, 2012:

	Fair Value Measurement Using		
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Total
Fair values as of January 31, 2012			
Assets:			
Money market funds	\$ 31,614	\$ —	\$31,614
Commercial paper	—	30,480	30,480
Corporate debt securities	—	20,983	20,983
U.S. agency notes	—	900	900
Total assets measured at fair value	<u>\$ 31,614</u>	<u>\$ 52,363</u>	<u>\$83,977</u>
Fair values as of April 30, 2012			
Assets:			
Money market funds	\$ 34,780	\$ —	\$34,780
Commercial paper	—	28,288	28,288
Corporate debt securities	—	9,607	9,607
U.S. agency notes	—	2,504	2,504
Total assets measured at fair value	<u>\$ 34,780</u>	<u>\$ 40,399</u>	<u>\$75,179</u>

The Company's money market funds are classified as Level 1 within the fair value hierarchy because they are valued primarily using quoted market prices. The Company's other cash equivalents and short-term investments are classified as Level 2 within the fair value hierarchy because they are valued using professional pricing sources for identical or comparable instruments, rather than direct observations of quoted prices in active markets.

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

**5. Commitments and Contingencies**

***Legal Proceedings***

Pandora has been in the past, and continues to be, a party to privacy and patent infringement litigation which has consumed, and may continue to consume, financial and managerial resources. The Company is also from time to time subject to various other legal proceedings and claims arising in the ordinary course of its business. Management believes that the liabilities associated with these cases, while possible, are not probable, and therefore the Company has not recorded any accrual for these as of January 31, 2012 and April 30, 2012. Further, any possible range of loss cannot be reasonably estimated at this time. The Company does not believe the ultimate resolution of any pending legal matters is likely to have a material adverse effect on its business, financial position, results of operations or cash flows.

In June 2011, a putative class action lawsuit was filed against Pandora in the United States District Court for the Northern District of California alleging that it unlawfully accessed and transmitted personally identifiable information of the plaintiffs in connection with their use of the Company's Android mobile application. In addition to civil liability, the amended complaint includes allegations of violations of statutes under which criminal penalties could be imposed if the Company were found liable. Pandora's motion to dismiss the first amended complaint was filed on March 23, 2012. No hearing date is currently set.

In September 2011, a putative class action lawsuit was filed against Pandora in the United States District Court for the Northern District of California alleging that it violated Michigan's video rental privacy law and consumer protection statute by allowing Pandora listeners' listening history to be visible to the public. Pandora's motion to dismiss the complaint was filed on November 28, 2011. No hearing date is currently set.

In April 2011, Augme Technologies, Inc. filed a complaint in the United States District Court for the District of Delaware against Pandora alleging patent infringement. The complaint alleges that Pandora infringes an Augme patent and seeks injunctive relief and monetary damages.

The Company currently believes that it has substantial and meritorious defenses to the claims in the lawsuits discussed above and intends to vigorously defend its position.

On December 29, 2011, Hartford Casualty Insurance Company filed a complaint in the U.S. District Court for the Northern District of California seeking a declaratory judgment that it has no obligation to defend or indemnify Pandora in relation to certain pending and formerly pending privacy class actions. Pandora and Hartford entered into a settlement agreement with respect to Hartford's claims on May 18, 2012.

The outcome of any litigation is inherently uncertain. Based on the Company's current knowledge it believes that the final outcome of the matters discussed above will not likely, individually or in the aggregate, have a material adverse effect on its business, financial position, results of operations or cash flows; however, in light of the uncertainties involved in such matters, there can be no assurance that the outcome of each case or the costs of litigation, regardless of outcome, will not have a material adverse effect on the Company's business.

***Guarantees and Contingencies***

The Company is party to certain contractual agreements under which it has agreed to provide indemnifications of varying scope and duration for claims by third parties relating to its intellectual property. Such indemnification provisions are accounted for in accordance with guarantor's accounting and disclosure requirements for guarantees, including indirect guarantees of indebtedness of others. To date, the Company has not incurred, does not anticipate incurring and therefore has not accrued for, any costs related to such indemnification provisions.

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

**6. Income Taxes**

For the three months ended April 30, 2012 the Company recorded a tax benefit of \$6,000 compared to a tax expense of \$22,000 for the three months ended April 30, 2011. The effective tax rate for the three months ended April 30, 2012 was less than one percent based on the estimated tax loss for the fiscal year.

There were no material changes to the unrecognized tax benefits in the three months ended April 30, 2012 and the Company does not expect significant changes to unrecognized tax benefits through the end of the fiscal year. Because of the Company's history of tax losses, all years remain open to tax audit.

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

**7. Debt Instruments**

On May 13, 2011, the Company entered into a \$30 million credit facility with a syndicate of financial institutions. The amount of borrowings available under the credit facility at any time is based on the Company's monthly accounts receivable balance at such time, and the amounts borrowed are collateralized by the Company's personal property (including such accounts receivable but excluding intellectual property). Under the credit facility, the Company can request up to \$5 million in letters of credit be issued by the financial institutions.

The credit facility contains customary events of default, conditions to borrowing and covenants, including restrictions on the Company's ability to dispose of assets, make acquisitions, incur debt, incur liens and make distributions to stockholders. The credit facility also includes a financial covenant requiring the maintenance of minimum liquidity of at least \$5 million. During the continuance of an event of a default, the lenders may accelerate amounts outstanding, terminate the credit facility and foreclose on all collateral.

As of April 30, 2012, the Company had \$520,000 in letters of credit outstanding and had \$29.48 million of available borrowing capacity under the credit facility. On December 30, 2011, the Company entered into a cash collateral agreement in connection with the issuance of letters of credit which were used to satisfy deposit requirements under facility leases. As of April 30, 2012, the \$520,000 cash collateral was considered to be restricted cash. The amount is included in other assets on the Company's balance sheet.

Total debt issuance costs associated with the credit facility were \$1.0 million, which are being amortized as interest expense over the four-year term of the credit facility agreement. For the three months ended April 30, 2012, \$0.1 million of debt issuance costs were amortized and included in interest expense.

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

**8. Stock-based Compensation Plans and Awards**

The Company's 2011 Equity Incentive Plan (the "2011 Plan") provides for the issuance of stock options, restricted stock units and other stock-based awards. Each fiscal year, (beginning with the fiscal year that commenced February 1, 2012 and ending with the fiscal year commencing February 1, 2021), the number of shares in the reserve under the 2011 Plan may be increased by the lesser of (x) 10,000,000 shares, (y) 4.0% of the outstanding shares of common stock on the last day of the prior fiscal year or (z) another amount determined by the Company's board of directors. The 2011 Plan is scheduled to terminate in 2021, unless the board of directors determines otherwise. The 2011 Plan is administered by the compensation committee of the board of directors of the Company.

**Valuation of Awards**

The per-share fair value of each stock option with a service period condition but not a market condition was determined on the date of grant using the Black-Scholes option pricing model using the following assumptions:

	Three Months Ended April 30,	
	2011	2012
Expected life (in years)	5.72-7.02	6.67
Risk-free interest rate	2.28%-3.30%	1.52%
Expected volatility	54%-57%	56%
Expected dividend yield	0%	0%

**Stock Options**

A summary of stock option activity for the three months ended April 30, 2012 is as follows:

	Options Outstanding Stock Options	Weighted- Average Exercise Price	Aggregate <sup>(1)</sup> Intrinsic Value
(in thousands, except share and per share data)			
Balance as of January 31, 2012	34,810,926	\$ 2.43	\$ 379,355
Granted	1,350,000	10.63	
Exercised	(2,750,045)	0.70	
Cancelled	(182,925)	4.00	
Balance as of April 30, 2012	<u>33,227,956</u>	\$ 2.90	<u>\$ 209,017</u>
Equity awards available for grant at April 30, 2012	<u>13,726,781</u>		

(1) Amounts represent the difference between the exercise price and the fair value of common stock at period end for all in the money options outstanding based on the fair value per share of common stock.



[Table of Contents](#)

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

*Restricted Stock Units*

The fair value of the restricted stock units (“RSUs”) is expensed ratably over the vesting period. RSUs vest annually on a cliff basis over the service period, generally four years. The Company recorded stock-based compensation expense related to RSUs of approximately \$1.8 million during the three months ended April 30, 2012. As of April 30, 2012, total compensation cost not yet recognized of approximately \$37.1 million related to non-vested RSUs, is expected to be recognized over a weighted average period of 3.68 years.

The following table summarizes the activities for our RSUs for the three months ended April 30, 2012:

	Number of Shares	Weighted- Average Grant-Date Fair Value
Unvested at January 31, 2012	1,426,975	\$ 12.03
Granted	1,932,762	11.94
Vested	—	—
Canceled	(24,775)	13.93
Unvested at April 30, 2012	<u>3,334,962</u>	\$ 11.95

*Stock Option Awards with Both a Service Period and a Market Condition*

On March 22, 2012 Mr. Joseph Kennedy, the Company’s Chief Executive Officer, was granted a non-statutory stock option to purchase 800,000 shares of common stock. This option grant to Mr. Kennedy was intended to be in lieu of an annual equity grant for fiscal 2014. This option includes both a service period and a market vesting condition. The stock option will vest if the 60-day trailing volume weighted average price of the Company’s common stock exceeds \$21.00 per share, or if there is a sale of the Company for at least \$21.00 per share, in each case prior to July 6, 2017. If the market condition is met, the performance option will vest ratably over four years, beginning on July 6, 2013, subject to severance and change of control acceleration. To the extent that the market condition is not met, the option will not vest and will be cancelled. The Company used a binomial model to value the option with a market condition. The Company used Monte Carlo simulation techniques that incorporate assumptions as provided by management for the term of option from grant date (in years), risk-free interest rate, stock price volatility and beginning stock price. The Company does not adjust compensation cost recognition for subsequent changes in the expected outcome of the market-vesting conditions.

The following assumptions were used to value the grant using the Monte-Carlo simulation option pricing model: 10-year term, risk-free interest rate of 2.33%, expected volatility of 70% and a beginning stock price of \$10.63. The grant-date fair value for the option was \$6.08. As of April 30, 2012, total compensation cost not yet recognized of approximately \$4.7 million related to this grant, is expected to be recognized over a period of 5.2 years.

*Stock-based Compensation Expenses*

The weighted-average fair value of stock option grants made during the three months ended April 30, 2011 and 2012 was \$3.21 and \$6.02, respectively. As of April 30, 2012, total compensation cost related to stock options granted, but not yet recognized, was \$46.4 million which the Company expects to recognize over a weighted-average period of approximately 2.68 years.

The total grant date fair value of stock options vested during the three months ended April 30, 2011 and 2012 was \$0.8 million and \$3.4 million, respectively. The aggregate intrinsic value of all options and warrants exercised during the three months ended April 30, 2011 and 2012 was \$2.4 million and \$32.4 million, respectively.

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[Table of Contents](#)

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

Stock-based compensation expenses related to all employee and non-employee stock-based awards was as follows (in thousands):

	Three Months Ended	
	April 30,	
	2011	2012
	(unaudited)	
Stock-based compensation expenses:		
Cost of revenue	\$ 64	\$ 263
Product development	177	986
Marketing and sales	423	2,930
General and administrative	272	1,321
Total stock-based compensation, recorded in costs and expenses <sup>(1)</sup>	\$ 936	\$ 5,500

[Table of Contents](#)

**Pandora Media, Inc.**

**Notes to Condensed Consolidated Financial Statements - Continued**

**9. Net Loss Per Share**

Basic net loss per share is computed by dividing the net loss by the weighted-average number of shares of common stock outstanding during the period.

Diluted net income per share is computed by giving effect to all potential shares of common stock, including stock options, restricted stock units, convertible preferred stock warrants and redeemable convertible preferred stock, to the extent dilutive. Basic and diluted net loss per share was the same for the three months ended April 30, 2011 and 2012 as the inclusion of all potential common shares outstanding would have been anti-dilutive.

The following table sets forth the computation of historical basic and diluted net loss per share (in thousands except per share amounts):

	Three Months Ended	
	April 30,	
	2011	2012
<b>Numerator</b>		
Net loss	\$ (6,754)	\$ (20,228)
Accretion of redeemable convertible preferred stock	(70)	—
Increase in cumulative dividends payable upon conversion or liquidation of redeemable convertible preferred stock	(2,320)	—
Net loss attributable to common stockholders	<u>\$ (9,144)</u>	<u>\$ (20,228)</u>
<b>Denominator</b>		
Weighted-average common shares outstanding used in computing basic and diluted net loss per share	<u>14,900</u>	<u>165,404</u>
Net loss per share, basic and diluted	<u>\$ (0.61)</u>	<u>\$ (0.12)</u>

Net loss was increased by the cumulative dividends payable upon conversion or liquidation of redeemable convertible preferred shares earned during the period to arrive at net loss attributable to common stockholders for the three months ended April 30, 2011. Dividends were accrued up through the conversion at the close of the IPO in June, 2011.

The following potential common shares outstanding were excluded from the computation of diluted net loss per share because including them would have been anti-dilutive (in thousands):

	Three Months Ended	
	April 30, 2011	April 30, 2012
Options to purchase common stock	37,633	33,228
Warrants to purchase convertible preferred stock	403	—
Restricted stock units	—	3,335
Convertible preferred stock	<u>137,295</u>	<u>—</u>
Total common stock equivalents	<u>175,331</u>	<u>36,563</u>

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*You should read the following discussion of our financial condition and results of operations in conjunction with the condensed consolidated financial statements and the notes thereto included elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the fiscal year ended January 31, 2012 filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act"). All references herein to a fiscal year refer to the 12 months ended January 31 of such year, and references to the first, second, third and fourth fiscal quarters refer to the three months ended April 30, July 31, October 31 and January 31, respectively.*

*This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve substantial risks and uncertainties. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Exchange Act, including, but not limited to, statements regarding our expectations, beliefs, intentions, strategies, future operations, future financial position, future revenue, projected expenses and plans and objectives of management. In some cases, you can identify forward-looking statements by terms such as "anticipate," "believe," "estimate," "expect," "intend," "may," "might," "plan," "project," "will," "would," "should," "could," "can," "predict," "potential," "continue," "objective," or the negative of these terms, and similar expressions intended to identify forward-looking statements. However, not all forward-looking statements contain these identifying words. These forward-looking statements reflect our current views about future events and involve known risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievement to be materially different from those expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" included in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the fiscal year ended January 31, 2012. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements. We qualify all of our forward-looking statements by these cautionary statements. These and other factors could cause our results to differ materially from those expressed in this Quarterly Report on Form 10-Q.*

*Some of the industry and market data contained in this Quarterly Report on Form 10-Q are based on independent industry publications, including those generated by Triton Digital Media or ("Triton") or other publicly available information. This information involves a number of assumptions and limitations. Although we believe that each source is reliable as of its respective date, we have not independently verified the accuracy or completeness of this information.*

*As used herein, "Pandora," the "Company," "we," "our," and similar terms refer to Pandora Media, Inc., unless the context indicates otherwise.*

*"Pandora" and other trademarks of ours appearing in this report are our property. This report may contain additional trade names and trademarks of other companies. We do not intend our use or display of other companies' trade names or trademarks to imply an endorsement or sponsorship of us by such companies, or any relationship with any of these companies.*

### Overview

Pandora is the leader in internet radio in the United States, offering a personalized experience for each of our listeners. We have pioneered a new form of radio – one that uses intrinsic qualities of music to initially create stations and then adapts playlists in real-time based on the individual feedback of each listener. As of April 30, 2012, we had approximately 150 million registered users, which we define as the total number of accounts that have been created for our service at period end. As of April 30, 2012 approximately 100 million registered users have accessed Pandora through smartphones and tablets. For the three months ended April 30, 2012, we streamed 3.09 billion hours of radio and as of April 30, 2012, we had 51.9 million active users during the prior 30 day period. According to a March 2012 report by Triton, we have more than a 70% share of internet radio among the top 20 stations and networks in the United States. Since we launched our free, advertising-supported radio service in 2005 our listeners have created over 2.8 billion stations.

Since we started the Music Genome Project in 2000, we have continuously built our song catalog, refined the genotyping model and developed proprietary algorithms for building personalized playlists for our listeners based both on our analysis and feedback data from our listeners.

Our comedy service leverages similar technology to the technology underlying the Music Genome Project, allowing a listener to choose a favorite comedian or a genre as a seed to start a station and then give feedback to personalize that station.

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## Table of Contents

The mobile version of our Pandora service, the Pandora app, is available for smartphones including the iPhone, Android and Blackberry phones, and for tablets including the iPad, Android tablets and Blackberry Playbook.

One key element of our strategy is to make the Pandora service available everywhere in the United States that there is internet connectivity. To this end, we partner with manufacturers of home entertainment systems and other consumer electronics products to integrate the Pandora service with their products. We also develop relationships with major automobile manufacturers and their suppliers to integrate the Pandora service with automobiles. We are currently available on models of Ford, Lincoln, Mercedes-Benz, MINI, BMW, Hyundai, Scion, Toyota, Lexus, Chevrolet, Buick, GMC and Honda. Additionally, Cadillac, Suzuki, Nissan and Kia have publicly announced their plans for future Pandora integrations.

### **Business Model**

We derive the substantial majority of our revenue from the sale of display, audio and video advertising for delivery across our traditional computer-based, mobile and other connected device platforms. We also offer a paid subscription service to listeners, which we call Pandora One. While historically our revenue growth was principally attributable to selling display advertising through our traditional computer-based platform, the rapid adoption of our service on mobile and other connected devices is changing this mix. This expansion of our services also presents an opportunity for us to reach our audience anytime, anywhere they enjoy music, and therefore offer additional distribution channels to current and potential advertisers for delivery of their advertising messages.

Growth in our active users and distribution platforms has fueled a corresponding growth in listener hours. Our total number of listener hours is a key driver for both revenue generation opportunities and content acquisition expenses, which are the largest component of our operating expenses:

- *Revenue.* Listener hours define the number of opportunities we have to sell advertisements, which we refer to as inventory. Our ability to attract advertisers depends in large part on our ability to offer sufficient inventory within desired demographics. In turn, our ability to generate revenue depends on the extent to which we are able to sell the inventory we have.
- *Content Acquisition Expenses.* Listener hours drive substantially all of our content acquisition expenses. With respect to each sound recording streamed to each listener, we pay royalties to the copyright owners both of sound recordings and of the underlying musical works, subject to certain exclusions, and we record these royalties as content acquisition expenses. Under U.S. law, we are guaranteed the right to stream any lawfully released sound recordings. Royalties for sound recordings are negotiated with and paid through SoundExchange. Royalties for musical works are negotiated with and paid through publishing companies such as Entertainment World Inc. or EMI; or performance rights organizations such as the American Society of Composers, Authors and Publishers, or ASCAP; Broadcast Music, Inc., or BMI; and SESAC Inc. or SESAC. Royalties are calculated using negotiated rates documented in master royalty agreements and based on sound recordings streamed, revenue earned or other usage measures. If we cannot agree on royalty rates, the dispute will be resolved by the Copyright Royalty Board, or CRB, in the case of SoundExchange, and by the rate court in the case of ASCAP and BMI. In May 2011, we started streaming spoken word comedy content, for which the underlying literary works are not currently entitled to eligibility for licensing by any performing rights organization for the United States. Rather, pursuant to industry-wide custom and practice, this content is performed absent a specific license from any such performing rights organization, however we pay royalties to SoundExchange at federally negotiated rates for the right to stream this spoken word comedy content.

Given the royalty structures in effect with respect to content acquisition, our content acquisition costs increase with each additional listener hour, subject to certain exclusions, regardless of whether we are able to generate more revenue. As such, our ability to achieve operating leverage depends on our ability to increase our revenue per hour of streaming through increased advertising sales.

As our mobile listenership increases, we face new challenges in optimizing our advertising products for delivery on mobile and other connected device platforms. The mobile advertising market is nascent and faces technical challenges due to fragmented platforms and lack of standard audience measurement protocols.

In addition, we expect to increase the number of audio ad campaigns for both traditional computer-based and mobile platforms, placing us in more direct competition with broadcast radio for advertiser spending, and these advertisers predominantly focus on local advertising. By contrast, display advertisers have been predominantly national brands. To successfully sell audio ads, we may have to convince a substantial base of local advertisers of the benefits of advertising on the Pandora service.

In fiscal 2011 and 2012, we substantially increased our expenditures for product development, marketing and sales and general and administrative expenses to generate growth and provide support infrastructure for that anticipated growth. We expect increased levels of operating expenses into the future.

Our total revenue has grown from \$51.0 million in the three months ended April 30, 2011 to \$80.8 million in the three months ended April 30, 2012. At the same time, our total cost and expenses have grown from \$56.2 million in the three months ended April 30,

## [Table of Contents](#)

2011 to \$100.9 million in the three months ended April 30, 2012, principally as a result of the growth in content acquisition expenses. As the volume of music we stream to listeners increases, our content acquisition expense will also increase, regardless of whether we are able to generate more revenue. In addition, we expect to invest heavily in our operations to support anticipated future growth. As a result of these factors, we expect to continue to incur operating losses on an annual basis through at least the end of fiscal 2013.

### **Key Metrics:**

We track listener hours because it is a key indicator of the growth of our business. We also track the number of active users as an additional indicator of the breadth of audience we are reaching at a given time, which is particularly important to potential advertisers.

We calculate listener hours based on the total bytes served for each track that is requested and served from our servers, as measured by our internal analytics systems, whether or not a listener listens to the entire track. We believe this server-based approach is the best methodology to forecast advertising inventory given that advertisements are frequently served in between tracks and are often served upon triggers such as a listener clicking thumbs-down or choosing to skip a track. To the extent that third-party measurements of listener hours are not calculated using a similar server-based approach, the third-party measurements may differ from our measurements.

Active users are defined as the number of distinct registered users that have requested audio from our servers within the trailing 30 days to the end of the final calendar month of the period. The number of active users may overstate the number of unique individuals who actively use our service within a month as one individual may register for, and use, multiple accounts.

The tables below set forth our listener hours for the three months ended April 30, 2011 and 2012 and our active users as of January 31 and April 30, 2012.

	Three Months Ended April 30,	
	2011	2012
Listener hours (in billions)	1.61	3.09
	As of January 31, 2012	As of April 30, 2012
Active users (end of period, in millions)	47.6	51.9

### **Basis of Presentation**

#### **Revenue**

*Advertising Revenue.* We generate advertising revenue primarily from display, audio and video advertising, which is typically sold on a cost-per-thousand impressions, or CPM, basis. Advertising campaigns typically range from one to 12 months, and advertisers generally pay us based on a minimum number of impressions or the satisfaction of other criteria, such as click-throughs. We may earn referral revenue when, for example, a listener clicks on an advertisement and signs up for membership with an advertiser. We also have arrangements with advertising agencies and brokers pursuant to which we provide the ability to sell advertising inventory on our service directly to advertisers. We report revenue under these arrangements net of amounts due to agencies and brokers.

For the three months ended April 30, 2011 and 2012, respectively, advertising revenue accounted for 86% and 87% of our total revenue. We expect that advertising will comprise a substantial majority of revenue for the foreseeable future.

*Subscription Services and Other Revenue.* We generate subscription revenue through the sale and activation of access to a premium version of the Pandora service for \$36 per year or, on some devices, \$4 per month, which currently includes an ad free environment and, on devices that support it, higher quality audio. We receive the full amount of the subscription payment, net of any applicable commissions and processing fees at the time of sale; however, subscription revenue is recognized on a straight-line basis over the subscription period. For the three months ended April 30, 2011 and 2012, subscription services and other revenue accounted for 14% and 13%, respectively, of our total revenue.

*Deferred Revenue.* Our deferred revenue consists principally of both prepaid but unrecognized subscription revenue and advertising fees received or billed in advance of the delivery or completion of the delivery of services. Deferred revenue is recognized as revenue when the services are provided and all other revenue recognition criteria have been met.

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## Table of Contents

### *Costs and Expenses*

Costs and expenses consist of cost of revenue, product development, marketing and sales, general and administrative and content acquisition expenses. Content acquisition expenses are the most significant component of our costs and expenses followed by employee-related costs, which includes stock-based compensation expenses. We expect to continue to hire employees in order to support our anticipated growth. In any particular period, the timing of additional hires could materially affect our operating expenses, both in absolute dollars and as a percentage of revenue. We anticipate that our costs and expenses will increase in the future.

*Cost of Revenue.* Cost of revenue consists of hosting costs, infrastructure and the employee and employee-related costs associated with supporting those functions. Hosting costs consist of content streaming, maintaining our internet radio service and creating and serving advertisements through third-party ad servers. Infrastructure costs consist of equipment, software, facilities and depreciation. We make payments to third-party ad servers for the period the advertising impressions or click-through actions are delivered or occur, and accordingly, we record this as a cost of revenue in the related period.

*Product Development.* Product development expenses consist of employee compensation, information technology, consulting, facilities-related expenses and costs associated with supporting consumer connected-device manufacturers in implementing our service in their products. We incur product development expenses primarily for improvements to our website and the Pandora app, development of new advertising products and development and enhancement of our personalized station(s) generating system. We have generally expensed product development as incurred. Certain website development and internal use software development costs may be capitalized when specific criteria are met. In such cases, the capitalized amounts are amortized over the useful life of the related application once the application is placed in service. We intend to continue making significant investments in developing new products and enhancing the functionality of our existing products.

*Marketing and Sales.* Marketing and sales expenses consist of employee and employee-related costs including salaries, commissions and benefits related to employees in sales, marketing and advertising departments. In addition, marketing and sales expenses include external sales and marketing expenses such as third-party marketing, branding, advertising and public relations expenses, and infrastructure costs such as facility and other supporting overhead costs. We expect marketing and sales expenses to increase as we hire additional personnel to build out our sales force and ad operations team and expand our business development team to establish relationships with manufacturers of an increasing number of connected devices.

*General and Administrative.* General and administrative expenses include employee and employee-related costs consisting of salaries and benefits for finance, accounting, legal, internal information technology and other administrative personnel. In addition, general and administrative expenses include professional services costs for outside legal and accounting services, and infrastructure costs for facility, supporting overhead costs and merchant and other transaction costs, such as credit card fees. We expect to incur additional expenses in future periods as we continue to invest in corporate infrastructure, including adding personnel and systems to our finance and administrative functions. We expect to continue to incur expenses associated with being a public company, including increased legal and accounting costs, investor relations costs and compliance costs in connection with section 404 of the Sarbanes-Oxley Act.

*Content Acquisition.* Content acquisition expenses principally consist of royalties payable for streaming music or other content to our listeners. Royalties are calculated using negotiated rates documented in master royalty agreements and are based on both percentage of revenue and listener metrics. The majority of our royalties are payable based on a fee per track, while in other cases our royalties are payable based on a percentage of our revenue.

We periodically test our royalty calculation methods to ensure we are accurately reporting and paying royalties. The performance rights organizations have the right to audit our playlist and payment records, and any such audit could result in disputes over whether we have paid the proper royalties. If such a dispute were to occur, we could be required to pay additional royalties, and the amounts involved could be material.

For royalty arrangements under negotiation, we accrue for estimated royalties based on the available facts and circumstances and adjust these estimates as more information becomes available. The results of any finalized negotiation may be materially different from our estimates.

In 2009 we, together with other webcasters, negotiated new royalty rates on performances with SoundExchange for calendar years 2006 to 2015. The agreement reduced rates originally established by the Copyright Royalty Board for calendar years 2006 to 2010 and established new rates for calendar years 2011 to 2015.

*Provision for Income Taxes.* Since our inception, we have been subject to income taxes only in the United States. In the event we expand our operations outside the United States, we will become subject to taxation based on the foreign statutory rates and our effective tax rate could fluctuate accordingly.

Income taxes are computed using the asset and liability method, under which deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted statutory income tax rates in effect for the year in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce net deferred tax assets to the amount expected to be realized.



## [Table of Contents](#)

### Results of Operations

The following table presents our results of operations for the periods indicated as a percentage of total revenue. The period-to-period comparisons of results are not necessarily indicative of results for future periods.

	Three Months Ended April 30,	
	2011 <sup>(2)</sup>	2012 <sup>(2)</sup>
	(unaudited)	
Revenue:		
Advertising	86%	87%
Subscription services and other	14	13
Total revenue	100	100
Costs and expenses:		
Cost of revenue <sup>(1)</sup>	9	9
Product development <sup>(1)</sup>	5	5
Marketing and sales <sup>(1)</sup>	25	29
General and administrative <sup>(1)</sup>	14	13
Content acquisition	57	69
Total costs and expenses	110	125
Loss from operations	(10)	(25)
Other income (expense):		
Interest income	—	—
Interest expense	—	—
Other expense, net	(3)	—
Loss before provision for income taxes	(13)	(25)
Provision for income taxes	—	—
Net Loss	(13)%	(25)%

(2) Amounts may not sum due to rounding.

(1) Includes stock-based compensation as follows:

Cost of revenue	0.1%	0.3%
Product development	0.3	1.2
Marketing and sales	0.8	3.6
General and administrative	0.5	1.6

### Comparison of the Three Months Ended April 30, 2011 and 2012

#### Revenue

	Three Months Ended April 30,		\$ Change
	2011	2012 (in thousands)	
Advertising	\$43,661	\$70,597	\$26,936
Subscription services and other	7,379	10,187	2,808
Total revenue	\$51,040	\$80,784	\$29,744

Three months ended 2011 compared to 2012. Advertising revenue increased \$26.9 million due to an increase in the number of advertising campaigns enabled by higher listener hours across our traditional computer as well as mobile and other connected device platforms, and by an increase in the size of our sales force as compared to the prior year period. Subscription revenue increased \$2.8 million due to an increase in the number of subscribers.



## Table of Contents

### *Costs and Expenses*

#### *Cost of Revenue*

	Three Months Ended April 30,		<u>\$ Change</u>
	<u>2011</u>	<u>2012</u> (in thousands)	
Cost of revenue	\$ 4,360	\$ 6,917	\$ 2,557

Three months ended 2011 compared to 2012. Cost of revenue increased \$2.6 million primarily due to a \$0.9 million increase in hosting services costs as a result of a 92% increase in listener hours, \$0.8 million higher employee-related expenses driven primarily by a 45% increase in headcount and \$0.6 million due to higher infrastructure costs.

#### *Product Development*

	Three Months Ended April 30,		<u>\$ Change</u>
	<u>2011</u>	<u>2012</u> (in thousands)	
Product development	\$ 2,731	\$ 4,119	\$ 1,388

Three months ended 2011 compared to 2012. Product development expenses increased \$1.4 million primarily due to \$1.5 million higher employee-related expenses driven by a 30% increase in headcount, partially offset by lower professional services fees.

#### *Marketing and Sales*

	Three Months Ended April 30,		<u>\$ Change</u>
	<u>2011</u>	<u>2012</u> (in thousands)	
Marketing and sales	\$ 12,964	\$ 23,460	\$ 10,496

Three months ended 2011 compared to 2012. Marketing and sales expenses increased \$10.5 million primarily due to an \$8.7 million increase in employee-related expenses driven by a 75% increase in headcount along with an increase in external sales and marketing expenses of \$1.2 million related to marketing events and marketing research.

#### *General and Administrative*

	Three Months Ended April 30,		<u>\$ Change</u>
	<u>2011</u>	<u>2012</u> (in thousands)	
General and administrative	\$ 6,943	\$ 10,612	\$ 3,669

Three months ended 2011 compared to 2012. General and administrative expenses increased \$3.7 million primarily due to a \$2.4 million increase in employee-related expenses driven by a 44% increase in headcount and higher overall compensation, and a \$0.9 million increase in professional services fees.

#### *Content Acquisition*

	Three Months Ended April 30,		<u>\$ Change</u>
	<u>2011</u>	<u>2012</u> (in thousands)	
Content acquisition	\$ 29,158	\$ 55,818	\$ 26,660

Three months ended 2011 compared to 2012. Content acquisition expenses increased \$26.7 million due to increased royalty payments driven by increased listener hours, higher royalty rates due to scheduled rate increases and higher revenue.

## Table of Contents

### *Other Income (Expense)*

	Three Months Ended		\$ Change
	April 30,		
	2011	2012	
	(in thousands)		
Interest income	\$ 2	\$ 32	\$ 30
Interest expense	(109)	(124)	(15)
Other income (expense)	(1,509)	—	1,509
Total other expense	<u>\$ (1,616)</u>	<u>\$ (92)</u>	<u>\$ 1,524</u>

*Three months ended 2011 compared to 2012.* Total other expenses decreased \$1.5 million due to the absence in the 2012 period of expenses related to the remeasurement of the fair value of our preferred stock warrants which existed as of April 30, 2011 but were converted into shares of common stock upon the closing of our IPO on June 20, 2011.

### *Provision for Income Taxes*

*Three months ended 2011 compared to 2012.* For the three months ended April 30, 2012 the Company recorded a tax benefit of \$6,000 compared to a tax expense of \$22,000 for the three months ended April 30, 2011. The difference was primarily driven by changes in state tax statutes which resulted in lower tax obligations in some states.

### *Off-Balance Sheet Arrangements*

Our liquidity is not dependent on the use of off-balance sheet financing arrangements and as of April 30, 2012 we had no such arrangements. There has been no material change in our contractual obligations other than in the ordinary course of business since our fiscal year ended January 31, 2012.

### **Quarterly Trends**

Our operating results fluctuate from quarter to quarter as a result of a variety of factors. We expect our operating results to continue to fluctuate in future quarters.

Our results may reflect the effects of some seasonal trends in listener behavior due to increased internet usage and sales of media-streaming devices during certain vacation and holiday periods. For example, we expect to experience increased usage during the fourth quarter of each calendar year due to the holiday season, and in the first quarter of each calendar year due to increased use of media-streaming devices received as gifts during the holiday season. We may also experience higher advertising sales during the fourth quarter of each calendar year due to greater advertiser demand during the holiday season and lower advertising sales during the first quarter of each calendar year due to seasonally adjusted advertising demand. While we believe these seasonal trends have affected and will continue to affect our operating results, our trajectory of rapid growth may have overshadowed these effects to date. We believe that our business may become more seasonal in the future and that such seasonal variations in listener behavior may result in fluctuations in our financial results.

In addition, expenditures by advertisers tend to be cyclical and discretionary in nature, reflecting overall economic conditions, the economic prospects of specific advertisers or industries, budgeting constraints and buying patterns and a variety of other factors, many of which are outside our control. For example, an advertiser which accounted for more than 10% of our advertising revenue for the first two quarters of fiscal 2012 did not meet this threshold for the first quarter of fiscal 2013. As a result of these and other factors, the results of any prior quarterly or annual periods should not be relied upon as indications of our future operating performance.

### **Liquidity and Capital Resources**

As of April 30, 2012 we had cash, cash equivalents and short-term investments totaling \$80.6 million, which consisted of cash and money market funds held at major financial institutions, debt instruments of the U.S. government and its agencies, commercial paper and investment-grade corporate debt securities. Our principal uses of cash during the three months ended April 30, 2012 were funding our operations and capital expenditures.

### *Sources of Funds*

We believe, based on our current operating plan, that our existing cash and cash equivalents and available borrowings under our credit facility will be sufficient to meet our anticipated cash needs for at least the next 12 months.

## Table of Contents

From time to time, we may explore additional financing sources and means to lower our cost of capital, which could include equity, equity-linked and debt financing. In addition, in connection with any future acquisitions, we may require additional funding which may be provided in the form of additional debt, equity or equity-linked financing or a combination thereof. There can be no assurance that any additional financing will be available to us on acceptable terms.

*Credit Facility.* On May 13, 2011, we entered into a \$30 million credit facility with a syndicate of financial institutions. The amount of borrowings available under the credit facility at any time is based on our monthly accounts receivable balance at such time, and the amounts borrowed are collateralized by our personal property (including such accounts receivable but excluding intellectual property). Under the credit facility, we can request up to \$5 million in letters of credit be issued by the financial institutions.

As of April 30, 2012, the Company had \$520,000 in letters of credit outstanding and had \$29.48 million of available borrowing capacity under the credit facility. On December 30, 2011, the Company entered into a cash collateral agreement in connection with the issuance of letters of credit which were used to satisfy deposit requirements under facility leases. As of April 30, 2012, the \$520,000 cash collateral was considered to be restricted cash. The amount is included in other assets on the Company's balance sheet.

### *Capital Expenditures*

Consistent with previous periods, future capital expenditures will primarily focus on acquiring additional hosting and general corporate infrastructure. Based on current estimates, we believe that our anticipated capital expenditures will be adequate to implement our current plans.

### *Historical Trends*

The following table summarizes our cash flow data for the three months ended April 30, 2011 and 2012.

	Three Months Ended	
	April 30,	
	2011	2012
	(in thousands)	
	(unaudited)	
Net cash provided by (used in) operating activities	\$ 2,775	\$(10,580)
Net cash provided by (used in) investing activities	(2,086)	9,216
Net cash provided by (used in) financing activities	(19)	1,928

### *Operating Activities*

In the three months ended April 30, 2011, net cash provided by operating activities was \$2.8 million including our net loss of \$6.8 million and non-cash charges of \$3.2 million. In addition, cash inflows from changes in operating assets and liabilities included an increase in accrued royalties of \$3.0 million due to the timing of royalty payments and an increase in the number of listeners, an increase in accrued compensation of \$2.8 million related to higher employee bonus compensation due to higher revenue, and an increase in deferred revenue of \$1.5 million primarily related to an increase in customers purchasing subscriptions for Pandora One, partially offset by cash outflows of \$1.4 million in prepaid expenses and other assets primarily related to deferred costs associated with this offering.

In the three months ended April 30, 2012, net cash used in operating activities was \$10.6 million, including our net loss of \$20.2 million and non-cash charges of \$7.2 million. Net cash used in operating activities included \$3.8 million higher accounts receivable primarily due to increased billings, and \$2.4 lower accrued compensation due commission and bonus payments, partially offset by \$4.3 million higher accrued royalties due to an increase in listening hours and scheduled royalty rate increases, \$2.5 million higher deferred revenue due to an increase in customers purchasing subscriptions for Pandora One and a \$1.2 million reimbursement of leasehold improvement costs related to our Oakland, California facility.

### *Investing Activities*

Cash used in investing activities in the three months ended April 30, 2011 was \$2.1 million consisting primarily of capital expenditures for server equipment.

Cash provided by investing activities in the three months ended April 30, 2012 was \$9.2 million consisting of \$28.1 million in maturities of short-term investments, partially offset by \$17.6 million in purchases of short-term investments and \$1.2 million in capital expenditures primarily related to leasehold improvements.

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## [Table of Contents](#)

### *Financing Activities*

Cash used in financing activities in the three months ended April 30, 2011 was \$19,000 consisting of repayment of debt of \$0.2 million partially offset by proceeds from the issuance of common stock of \$0.1 million.

Cash provided by financing activities in the three months ended April 30, 2012 was \$1.9 million consisting of proceeds from issuance of common stock.

### **Critical Accounting Policies and Estimates**

Our discussion and analysis of our financial condition and results of operations is based upon our condensed consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and the related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances. Our estimates form the basis for our judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

An accounting policy is considered to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used, or changes in the accounting estimate that are reasonably likely to occur, could materially impact the condensed consolidated financial statements. We believe that our critical accounting policies reflect the more significant estimates and assumptions used in the preparation of the condensed consolidated financial statements.

There have been no material changes to our critical accounting policies and estimates as compared to those described in our Annual Report on Form 10-K for the fiscal year ended January 31, 2012 under the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Policies and Estimates.”

### **Item 3. Quantitative and Qualitative Disclosure About Market Risk**

There have been no material changes in our primary market risk exposures or how those exposures are managed from the information disclosed in Part II, Item 7A of our Annual Report on Form 10-K for the fiscal year ended January 31, 2012. For further discussion of quantitative and qualitative disclosures about market risk, reference is made to our Annual Report on Form 10-K.

### **Item 4. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

We maintain “disclosure controls and procedures,” as such term is defined in Rule 13a-15(e) under the Exchange Act, that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognizes that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. Based on their evaluation at the end of the period covered by this Quarterly Report on Form 10-Q, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of April 30, 2012.

#### **Changes in Internal Control over Financial Reporting**

There has been no change in our internal control over financial reporting during the three months ended April 30, 2012 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings**

The material set forth in Note 5 of Notes to Condensed Financial Statements in Part I, Item 1 of this Quarterly Report on Form 10-Q is incorporated herein by reference.

## Table of Contents

### **Item 1A. Risk Factors**

*Investing in our common stock involves a high degree of risk. Before deciding to invest in our common stock, you should carefully consider each of the risk factors described in “Part I - Item 1A. Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended January 31, 2012 and all information set forth in this Quarterly Report on Form 10-Q. Those risks and the risks described in this Quarterly Report on Form 10-Q, including in the section entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” could materially harm our business, financial condition, operating results, cash flow and prospects. If that occurs, the trading price of our common stock could decline, and you may lose all or part of your investment.*

There have been no material changes to the Risk Factors described under “Part I - Item 1A. Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended January 31, 2012, other than:

*If music publishers withdraw all or a portion of their digital music catalogs from performing rights organizations, we may be forced to enter into direct licensing agreements with these publishers at rates higher than those we currently pay, or we may be unable to reach agreement with these publishers at all, which could adversely affect our business, financial condition and results of operations.*

If music publishers withdraw all or a portion of their catalogs from performing rights organizations (or “PROs”) such as ASCAP, BMI or SESAC, we may no longer be able to obtain licenses for such publisher’s withdrawn catalogs. Under these circumstances, digital music webcasters, such as Pandora, who have been able to secure licenses for such publisher’s musical compositions would need to enter into direct licensing arrangements with music publishers. Although we continue to be licensed by the PROs, it is currently unclear what specific effect a publisher’s limited withdrawal from a PRO would have on us. For example, EMI withdrew its catalog from ASCAP in May 2011, and as a result we entered into a separate license agreement with EMI in March 2012. If we are unable to reach an agreement with respect to the repertoire of any music publisher who withdraws all or a portion of its catalog(s) from a PRO, or if we are forced to enter into direct licensing agreements with publishers at rates higher than those currently set by the PROs (or the U.S. District Court having supervisory authority over ASCAP and BMI) for the performance of musical works, our ability to stream music content to our listeners may be limited or our operating costs may significantly increase, which could adversely affect our business, financial condition and results of operations.

### **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

In June 2011, our registration statement on Form S-1 (File No. 333-172215) was declared effective for our initial public offering (“IPO”). There have been no changes regarding the use of proceeds from our IPO from the disclosure in our Annual Report on Form 10-K for the fiscal year ended January 31, 2012.

### **Item 6. Exhibits**

<u>Exhibit No.</u>	<u>Exhibit Description</u>	<u>Incorporated by Reference</u>			<u>Filed Herewith</u>	
		<u>Form</u>	<u>File No.</u>	<u>Exhibit</u>		<u>Filing Date</u>
10.19†	Offer Letter with Simon Fleming-Wood, dated August 5, 2011					X
10.20†	2013 Corporate Incentive Plan					X
10.21†	Stock Option Agreement with Joseph Kennedy, dated March 22, 2012					X
31.01	Certification of the Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act					X
31.02	Certification of the Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act					X
32.01	Certification of the Principal Executive Officer and Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act					X

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## Table of Contents

<u>Exhibit No.</u>	<u>Exhibit Description</u>	<u>Incorporated by Reference</u>					<u>Filed Herewith</u>
		<u>Form</u>	<u>File No.</u>	<u>Exhibit</u>	<u>Filing Date</u>	<u>Filed By</u>	
101	Interactive Data Files Pursuant to Rule 405 of Regulation S-T: (i) Condensed Balance Sheets as of April 30, 2012 and January 31, 2012, (ii) Condensed Statements of Operations for the Three Months ended April 30, 2012 and 2011, (iii) Condensed Statements of Cash Flows for the Three Months ended April 30, 2012 and 2011 and (iv) Notes to Condensed Financial Statements						X

† Indicates management contract or compensatory plan

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[Table of Contents](#)

**SIGNATURES**

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

**PANDORA MEDIA, INC.**

Date: June 1, 2012

By: /s/ Steven Cakebread

Steven Cakebread  
Executive Vice President and Chief  
Financial Officer

(Duly Authorized Officer and Principal Financial and  
Accounting Officer)

30

[\(Back To Top\)](#)

## **Section 2: EX-10.19 (OFFER LETTER WITH SIMON FLEMING-WOOD)**

**Exhibit 10.19**

**PANDORA**

internet radio

August 5, 2011

Simon Fleming-Wood  
Piedmont, CA 94610

Re: Employment Offer

Dear Simon:

On behalf of Pandora Media, Inc. (the "Company"), we are pleased to offer you the position of Chief Marketing Officer. This letter agreement sets forth the terms and conditions of your employment with the Company ("Agreement") if you accept and commence such employment. Please understand that this offer, if not accepted, will expire on August 12, 2011.

**1. Responsibilities; Duties.** You are expected to begin work on 10/12/2011 (the "Start Date"). You are required to faithfully and conscientiously perform your assigned duties and to diligently observe all your obligations to the Company. You agree to devote your full business time and efforts, energy and skill to your employment at the Company, and you agree to apply all your skill and experience to the performance of your duties and advancing Company's interests. During your employment with the Company, you may not perform services as an employee or consultant of any other organization and you will not assist any other person or organization in competing with the Company or in preparing to engage in competition with the business or proposed business of the Company. You shall comply with and be bound by Company's operating policies, procedures, and practices from time to time in effect during your employment.

**2. Compensation.** In consideration for rendering services to the Company during the term of your employment and fulfilling your obligations under this Agreement, you will be eligible to receive the benefits set forth in this Agreement.

a. **Base Salary.** In this exempt full-time position, you will earn an annual base salary of \$300,000 (prorated for any partial pay period that occurs during the term of your employment), subject to applicable tax withholdings. Your salary will be payable pursuant to the Company's regular payroll policy.

b. **Business Expenses.** The Company shall, upon submission and approval of written statements and bills in accordance with the then regular procedures of the Company, pay or reimburse you for any and all necessary, customary and usual expenses incurred by you while traveling for or on behalf of the Company, and any and all other necessary, customary or usual expenses (including entertainment) incurred by you for or on behalf of the Company in the normal course of business, as determined to be appropriate by the Company. It is your responsibility to review and comply with the Company's business expense reimbursement policies.

c. **Signing Bonus.** You will receive a special one-time signing bonus in the amount of \$50,000 (the "Sign-on Bonus"), less applicable tax withholdings, within 30 days following your Start Date. If your employment terminates prior to the first anniversary of your Start Date, you agree to repay the Sign-on Bonus in full and, in furtherance of such repayment agreement, authorize the Company to deduct the amount of the Sign-on Bonus from any other amounts that may be due to you; *provided* that if the Company terminates you without cause (as defined in the Company's

applicable severance policy) before such first anniversary, you will not be required to repay the Sign-on Bonus.

d. Performance Bonus. Your target bonus under the Company's bonus plan for the fiscal



year ending January 31, 2012 will be 40% of your base salary (prorated from your Start Date) and for the fiscal year ending January 31, 2013 will be 50% of your base salary. The actual bonus amount paid will be determined in the sole and absolute discretion of the Company's Compensation Committee. Any bonus eligibility for future years will be subject to the terms and conditions of any bonus or incentive compensation plan that the Company adopts at a later time. Nothing hereunder shall be construed or interpreted as a guarantee for you to receive any bonuses or incentive compensation.

**3. Employee Benefits.** You will be eligible to participate in any employee benefit plans or programs maintained or established by the Company including, but not limited to, paid time off, group health benefits, life insurance, dental plan, and other benefits made available generally to employees, subject to eligibility requirements and the applicable terms and conditions of the plan or program in question and the determination of any committee administering such plan or program. To the extent approved by the Board of Directors or its Compensation Committee from time to time, you will be eligible for any severance or change in control policy of the Company that is then applicable to similarly situated U.S. employees.

**4. Equity Grant.** In connection with the commencement of your employment, the Company will recommend that our Board of Directors (or its delegatee) grant you an award of restricted stock units (the "RSUs") representing a total of 200,000 shares of the Company's Common Stock, which will be delivered upon vesting of the corresponding RSUs. The RSUs will vest in 25% annual installments over four years starting with the first standard quarterly Company vesting date that is approximately one year after the grant date. Vesting will, of course, depend on your continued employment with the Company. The RSUs will be subject to the terms of the Company's equity incentive plan and the Restricted Stock Unit Agreement between you and the Company (together, the "Equity Plan Documents"). You understand that issuing the RSUs is expressly contingent on approval by our Board of Directors (or its delegatee).

**5. At-Will Employment.** Your employment with the Company will be on an "at will" basis, meaning that either you or the Company may terminate your employment at any time without notice and for any reason or no reason, without further obligation or liability. Further, your continued employment as well as your participation in any benefit programs does not assure you of continuing employment with the Company. The Company also reserves the right to modify or amend the terms of your employment, compensation and benefit plans at any time for any reason. This policy of at-will employment is the entire agreement as to the duration of your employment and may only be modified in an express written agreement signed by the Chief Executive Officer of the Company.

**6. Pre-employment Conditions.**

a. **Confidentiality Agreement.** Your acceptance of this offer and commencement of employment with the Company is contingent upon the execution, and delivery to an officer of the Company, of the Company's Confidential Information and Invention Assignment Agreement, a copy of which is enclosed for your review and execution (the "Confidentiality Agreement"), prior to or on your Start Date.

b. **Right to Work.** For purposes of federal immigration law, you will be required to provide to the Company documentary evidence of your identity and eligibility for employment in the United States. Such documentation must be provided to us no later than your Start Date, or our employment relationship with you may be terminated.

c. **Verification of Information.** This offer of employment is also contingent upon the successful verification of the information you provided to the Company during your application process, as well as a general background check performed by the Company to confirm your suitability for employment. By

accepting this offer of employment, you warrant that all information provided by you is true and correct to the best of your knowledge, and you expressly release all parties from any and all liability for damages that may result from obtaining, furnishing, collecting or verifying such information, as well as from the use of or disclosure of such information by the Company or its agents. You have a right to review copies of any public records obtained by the Company in conducting this verification process unless you check the box below.

I hereby waive my right to receive any public records as described above.

**7. No Conflicting Obligations.** You understand and agree that by accepting this offer of employment, you represent to the Company that performance of your duties to the Company and the terms of this Agreement and the Confidentiality Agreement will not breach any other agreement (written or oral) to which you are a party (including without limitation, current or past employers) and that you have not, and will not during the term of your employment with the Company, enter into any oral or written agreement which may result in a conflict of interest or may otherwise be in conflict with any of the provisions of this Agreement, the Confidentiality Agreement or the Company's policies. You are not to bring with you to the Company, or use or disclose to any person associated with the Company, any confidential or proprietary information belonging to any former employer or other person or entity with respect to which you owe an obligation of confidentiality under any agreement or otherwise. The Company does not need and will not use such information. Also, we expect you to abide by any obligations to refrain from soliciting any person employed by or otherwise associated with any former employer and suggest that you refrain from having any contact with such persons until such time as any non-solicitation obligation expires. To the extent that you are bound by any such obligations, you must inform the Company immediately prior to accepting this Agreement.

**8. General Obligations.** As an employee, you will be expected to adhere to the Company's standards of professionalism, loyalty, integrity, honesty, reliability and respect for all. Please note that the Company is an equal opportunity employer. The Company does not permit, and will not tolerate, the unlawful discrimination or harassment of any employees, consultants, or related third parties on the basis of sex, race, color, religion, age, national origin or ancestry, marital status, veteran status, mental or physical disability or medical condition, sexual orientation, pregnancy, childbirth or related medical condition, or any other status protected by applicable law. Any questions regarding this EEO statement should be directed to Human Resources.

**9. Termination Obligations.**

a. You agree that all property, including, without limitation, all equipment, proprietary information, documents, books, records, reports, notes, contracts, lists, computer disks (and other computer-generated files and data), and copies thereof, created on any medium and furnished to, obtained by, or prepared by you in the course of or incident to your employment, belongs to the Company and shall be returned to the Company promptly upon any termination of your employment, or sooner if so requested by the Company.

b. Upon your termination of your employment with the Company for any reason, if applicable, you will resign in writing (or be deemed to have resigned) from all other offices and directorships then held with the Company or any affiliate of the Company, unless otherwise agreed with the Company.

c. Following the termination of your employment with the Company for any reason, you shall fully cooperate with the Company in all matters relating to the winding up of pending work on behalf of the Company and the orderly transfer of work to other employees of the Company. You shall also cooperate in the defense of any action brought by any third party against the Company. If necessary, the Company shall pay you for your time incurred to comply with this provision at a reasonable per diem or per hour rate as to be determined by the Company.

d. Following the termination of your employment with the Company for any reason, you agree that you will not at any time make any statements or comments (written or oral) to any third party or take any action disparaging the integrity or reputation of the Company or any of its subsidiaries, employees, officers, directors, stockholders or affiliates. You also agree that you will not do or say anything that could disrupt the good morale of the employees of any of the companies listed above or harm their respective businesses or reputations of the companies and persons listed above.

## **10. Miscellaneous Terms.**

a. Entire Agreement. This Agreement, together with its Attachment A (the Confidentiality Agreement), set forth the entire terms of your employment with the Company (other than the Equity Plan Documents) and supersede any prior representations or agreements, whether written or oral.

b. Governing Law. This Agreement will be governed by the laws of California, without regard to its conflict of laws provisions. This Agreement may not be modified or amended except by a written agreement, signed by the CEO (or his authorized representative) of the Company.

c. Counterparts. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original but all of which shall together constitute one and the same instrument.

d. Severability. Nothing contained in this Agreement shall be construed as requiring the commission of any act contrary to law, and wherever there is any conflict between any provision of this Agreement and any present or future statute, law, ordinance or regulation contrary to which the parties have no legal right to contract, the latter shall prevail, but in such event, any provision of this Agreement thus affected shall be curtailed and limited only to the extent necessary to bring it within the requirements of the law. In the event that any part, article, paragraph or clause of this Agreement shall be held to be indefinite or invalid, the entire Agreement shall not fail on account thereof, and the balance of the Agreement shall continue in full force and effect.

e. Waiver. Failure or delay of either party to insist upon compliance with any provision hereof will not operate as, and is not to be construed as, a waiver or amendment of such provision or the right of the aggrieved party to insist upon compliance with such provision or to take remedial steps to recover damages or other relief for noncompliance. Any express waiver of any provision of this Agreement will not operate and is not to be construed as a waiver of any subsequent breach, whether occurring under similar or dissimilar circumstances.

We are all delighted to be able to extend you this offer and look forward to working with you. To indicate your acceptance of the Company's offer, please sign and date this Agreement in the space provided below and return it to me, along with a signed and dated original copy of the Confidentiality Agreement, prior to the expiration date specified in the opening paragraph of this Agreement.

Very truly yours,

PANDORA MEDIA, INC.

By: \_\_\_\_\_

Name: Joe Kennedy

Title: Chief Executive Officer

**ACCEPTED AND AGREED:**

I have read this offer and agree to accept employment with Company under the terms set forth in this Agreement.

Simon Fleming-Wood

/s/ Simon Fleming-Wood

Signature

8/10/2012

Date

Attachment A  
Confidential Information and Invention Assignment Agreement

6

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Oakland CA 94612

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[\(Back To Top\)](#)

## Section 3: EX-10.20 (2013 CORPORATE INCENTIVE PLAN)

Exhibit 10.20

### Pandora Media Corporate Incentive Plan for Fiscal Year 2013

The Pandora Media Inc. (“**Pandora**”) Corporate Incentive Plan for Fiscal Year 2013 (the “**Plan**”) is designed to reward eligible employees for their efforts toward the accomplishment of Pandora’s goals during the Plan Year. For purposes of the Plan, “**Plan Year**” means Pandora’s fiscal year starting February 1, 2012 through and including January 31, 2013, but, as further described below, eligible employees may receive a partial mid-year bonus.

#### Eligibility

**Eligibility under the Plan does not represent a commitment or guarantee that you will receive any payment under the Plan. If, for any reason, you are not an active Pandora employee on the bonus payment date, you will not be eligible to receive a bonus under the Plan.** Furthermore, the decision to pay any bonus under the Plan remains in the full discretion of the Compensation Committee of Pandora’s Board of Directors.

Selected employees at the manager or equivalent level and all employees at the director level and above are eligible (an “**Eligible Position**”). An eligible employee must remain an employee in good standing on the date that bonuses are paid to receive any payment under the Plan.

*New Hires and Promotions into Eligible Positions.* Eligible employees hired or promoted into an Eligible Position after February 2012 will have any bonus prorated to reflect the length of time employed in an Eligible Position during the Plan Year. However, employees hired after June 1, 2012 will not be eligible for a Mid-Year Bonus (as defined below), and employees hired after December 1, 2012 will not be eligible for the Plan.

*Changes Between Eligible Positions.* Eligible employees who move from one Eligible Position to another Eligible Position with a different Target Bonus will have any bonus prorated to reflect the different Target Bonus amounts based on the length of time employed in each Eligible Position.

#### Target Bonus Opportunity

Each Eligible Position is assigned a target bonus amount (“**Target Bonus**”), expressed as a percentage of earned salary for the applicable period. Your manager will discuss your Target Bonus with you.

#### Plan Administration

The Compensation Committee will have sole discretion to determine whether any percentage of Target Bonus will be paid under the Plan, in amounts ranging from 0% to over 100% of Target Bonus, depending solely upon its assessment of Pandora’s overall performance measured against objectives that the Compensation Committee and management will discuss from time to time. Pandora and the Compensation Committee may amend, suspend or terminate the Plan at any time and in any manner. **All payments under the Plan are discretionary and may be reduced or eliminated in the sole discretion of the Compensation Committee.**

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The Incentive Committee of Pandora (the “**Incentive Committee**”) is responsible for administering the Plan with respect to employees who are not executive officers (“**Non-Executive Employees**”), subject to the direction of the Compensation Committee. Members of the Incentive Committee include the Chief Financial Officer, General Counsel, and the Vice President of Human Resources. The Incentive Committee will, in its discretion, determine a Non-Executive Employee’s eligibility under the Plan, including whether part-time employees are eligible and whether Pandora will pay prorated bonuses for Non-Executive Employees who retire (and, if so, the retirement criteria) or die during the Plan Year. All determinations, interpretations, rules and decisions of the Compensation Committee and/or the Incentive Committee shall be conclusive and binding upon all persons claiming to have any interest or right under the Plan.

### **Bonus Payments**

In order to receive any payment under the Plan, an eligible employee must remain an active employee on the date that bonuses are paid. If, before a bonus payment date, your employment is terminated (whether by you or by Pandora, regardless of the reason), you will not be eligible to receive a bonus under the Plan.

Mid-Year Bonus – In the sole discretion of the Compensation Committee, a “**Mid-Year Bonus**” of up to 25% of each eligible employee’s Target Bonus may be paid during the year based on the Compensation Committee’s assessment of Pandora’s performance through July 31, 2012.

Year-End Bonus – A year-end bonus (with the percentage of Target Bonus determined by the Compensation Committee in its sole discretion) may be paid based on the Compensation Committee’s assessment of Pandora’s performance for the fiscal year ending January 31, 2013, less any Mid-Year Bonus previously paid.

If the Compensation Committee approves payment under this Plan, each eligible employees will receive the same percentage of his or her Target Bonus. However, the foregoing does not limit the Compensation Committee’s authority to award discretionary bonuses to individuals outside of the Plan.

### **Operating Guidelines**

No eligible employee may rely on any verbal or other information outside of this Plan. Pandora reserves the right to amend, discontinue or make significant changes to the Plan at any time and for any reason, with or without notice. Eligibility for a bonus under this Plan does not guarantee eligibility for any future payments or bonus programs.

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**At Will Employment**

Nothing in the Plan shall confer upon any employee or other Plan participant any right to continued employment or service with Pandora for any specific duration or otherwise restrict in any way the rights of Pandora or any employee to terminate an eligible employee's employment at any time, for any reason, with or without cause.

**Tax Withholding**

Pandora shall withhold from the payments under the Plan all federal, state and local income or other taxes required to be withheld therefrom and any other required payroll deductions, and as a condition precedent to payment under the Plan, all recipients shall make arrangements satisfactory to Pandora for the payment of any personal income or other taxes. All payments hereunder are intended to qualify for the short-term deferral exception from Section 409A of the Internal Revenue Code and, if required to qualify for such exception, shall be made no later than 2 and 1/2 months following the end of the taxable year in which an individual becomes legally entitled to, or vested in, a payment hereunder.

**Miscellaneous**

This Plan is unfunded. In no event may a participant sell, transfer, anticipate, assign or otherwise dispose of any right or interest under the Plan or relating hereto. At no time will any such right or interest under the Plan be subject to the claims of any participant's creditors or liable to attachment, execution or other legal process.

[\(Back To Top\)](#)

## **Section 4: EX-10.21 (STOCK OPTION AGREEMENT WITH JOSEPH KENNEDY)**

**Exhibit 10.21**

**PANDORA MEDIA, INC.**

**2011 Equity Incentive Plan**

**NOTICE OF PERFORMANCE-BASED STOCK OPTION GRANT (NSO)**

Joseph Kennedy

You have been granted an option to purchase Common Stock of Pandora Media, Inc. (the "Company") as follows:

Date of Grant:	March 22, 2012
Exercise Price per Share:	\$10.63
Total Number of Shares Granted:	800,000
Total Exercise Price:	\$8,504,000
Type of Option:	Nonstatutory Stock Option
Expiration Date:	March 22, 2022
Vesting Commencement Date:	July 6, 2013
Vesting/Exercise Schedule:	The Shares underlying this Option shall vest and become exercisable in accordance with the following schedule:

No portion of the Performance Option shall vest unless, during any period starting on the Date of Grant, the 60-day trailing volume weighted average price of the Company's stock is equal to or greater than \$21.00 (the "Performance Goal") (as adjusted for any stock split after the Date of Grant).

- If the Performance Goal is achieved for any such period starting on the Date of Grant, the Performance Option will be subject to monthly vesting over four years from the Vesting Commencement Date, such that the first vesting date shall be August 6, 2013 (the "Initial Vest Date"), if you remain in Continuous Service Status on each applicable vesting date.

- 
- If the Performance Goal is achieved after the Initial Vest Date, then the option shall be immediately vested to the extent the option would have been then vested if the vesting had begun on the Initial Vest Date.
  - If the Performance Goal is not achieved prior to the date that your Continuous Service Status ceases for any reason, the Performance Option shall be forfeited in its entirety, notwithstanding anything to the contrary in your offer letter or any Company severance policy, plan or agreement.

If the Performance Goal is not achieved on or before July 6, 2017, the Performance Option shall be forfeited in its entirety.

Change of Control:

If the Performance Goal is achieved on or prior to the date of consummation of a Change of Control, or if the per share value received by the Company's stockholders upon a Change of Control (as defined in the Company's equity incentive plan) is equal to or greater than \$21.00 (as adjusted for any stock split after the Date of Grant), the Performance Option shall be subject to any applicable accelerated vesting treatment for equity awards set forth in your offer letter or any other applicable Company policy, plan or agreement.

However, if the Performance Goal is not achieved on or prior to the date of consummation of a Change of Control and the per share value received by the Company's stockholders on such Change of Control is less than \$21.00 (as adjusted for any stock split after the Date of Grant), the Performance Option shall not be subject to any accelerated vesting treatment for equity awards set forth in your offer letter or any other applicable Company policy, plan or agreement and shall be forfeited immediately prior to consummation of such Change in Control.

Termination Period:

To the extent vested on the date of termination of your Continuous Service Status, this Option may



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be exercised for three months after termination of Continuous Service Status except as set out in Section 5 of the Stock Option Agreement (but in no event later than the Expiration Date). You are responsible for keeping track of these exercise periods following termination for any reason of your service relationship with the Company. The Company will not provide further notice of such periods.

Transferability:

This Option may not be transferred.

By accepting this Option, you agree that this Option is granted under and governed by the terms and conditions of the Pandora Media, Inc. 2011 Equity Incentive Plan and the Stock Option Agreement attached hereto and incorporated by reference herein.

In addition, you agree and acknowledge that your rights to any Shares underlying the Option will be earned only as you provide services to the Company over time, that the grant of the Option is not as consideration for services you rendered to the Company prior to your Vesting Commencement Date, and that nothing in this Notice or the attached documents confers upon you any right to continue your employment or consulting relationship with the Company for any period of time, nor does it interfere in any way with your right or the Company's right to terminate that relationship at any time, for any reason, with or without cause.

**PANDORA MEDIA, INC.**

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Joseph Kennedy

By: \_\_\_\_\_  
Name:  
Title:

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PANDORA MEDIA, INC.

2011 EQUITY INCENTIVE PLAN

STOCK OPTION AGREEMENT (NSO)

1. **Grant of Option.** Pandora Media, Inc., a Delaware corporation (the “Company”), hereby grants to Joseph Kennedy (“Optionee”), an option (the “Option”) to purchase the total number of shares of Common Stock (the “Shares”) set forth in the Notice of Stock Option Grant (the “Notice”), at the exercise price per Share set forth in the Notice (the “Exercise Price”) subject to the terms, definitions and provisions of the Pandora Media, Inc. 2011 Equity Incentive Plan (the “Plan”) adopted by the Company, which is incorporated in this Agreement by reference. Unless otherwise defined in this Agreement, the terms used in this Agreement shall have the meanings defined in the Plan.

2. **Designation of Option.** This Option is intended to be a Nonstatutory Stock Option.

3. **Exercise of Option.** This Option shall be exercisable during its term in accordance with the Vesting/Exercise Schedule set out in the Notice as follows:

(a) **Right to Exercise.**

(i) This Option may not be exercised for a fraction of a share.

(ii) In the event of Optionee’s death, disability or other termination of Continuous Service Status, the exercisability of the Option is governed by Section 5 below, subject to the limitations contained in this Section 3.

(iii) In no event may this Option be exercised after the Expiration Date of the Option as set forth in the Notice.

(b) **Method of Exercise.**

(i) This Option shall be exercisable by execution and delivery of a form of exercise notice (which may be written or electronic, as determined by the Company) approved for such purpose by the Company which shall state Optionee’s election to exercise the Option, the number of Shares in respect of which the Option is being exercised, and such other representations and agreements as to the holder’s investment intent with respect to such Shares as may be required by the Company. The notice shall be accompanied by payment of the Exercise Price. This Option shall be deemed to be exercised upon receipt by the Company of such written notice accompanied by the Exercise Price.

(ii) As a condition to the exercise of this Option, Optionee agrees to make adequate provision for federal, state or other tax withholding obligations, if any, which arise upon the vesting or exercise of the Option, or disposition of Shares, whether by withholding, direct payment to the Company, or otherwise.

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(iii) The Company is not obligated, and will have no liability for failure, to issue or deliver any Shares upon exercise of the Option unless such issuance or delivery would comply with the Applicable Laws, with such compliance determined by the Company in consultation with its legal counsel.

4. **Method of Payment.** Payment of the Exercise Price shall be by any of the following, or a combination of the following, at the election of Optionee:

(a) cash or check;

(b) cancellation of indebtedness;

(c) if the Common Stock is listed on an exchange or market, and if the Company is at such time permitting broker-assisted cashless exercises, delivery of a properly executed exercise notice together with irrevocable instructions to a broker participating in such cashless brokered exercise program to deliver promptly to the Company the amount required to pay the exercise price (and applicable withholding taxes) and in any event in accordance with applicable law;

(d) with respect to a Nonstatutory Option, such other method as may be approved by the Committee.

5. **Termination of Relationship.** Following the date of termination of Optionee's Continuous Service Status for any reason (the "Termination Date"), Optionee may exercise the Option only as set forth in the Notice and this Section 5. To the extent that Optionee is not entitled to exercise this Option as of the Termination Date, or if Optionee does not exercise this Option within the Termination Period set forth in the Notice or the termination periods set forth below, the Option shall terminate in its entirety. In no event, may any Option be exercised after the Expiration Date of the Option as set forth in the Notice.

(a) **Termination.** In the event of termination of Optionee's Continuous Service Status other than as a result of Optionee's disability or death, Optionee may, to the extent Optionee is vested in the Option Shares the date of such termination (the "Termination Date"), exercise this Option during the Termination Period set forth in the Notice.

(b) **Other Terminations.** In connection with any termination other than a termination covered by Section 5(a), Optionee may exercise the Option only as described below:

(i) **Termination upon Disability of Optionee.** In the event of termination of Optionee's Continuous Service Status as a result of Optionee's disability, Optionee may, but only within six months from the Termination Date, exercise this Option to the extent Optionee was vested in the Option Shares it as of such Termination Date.

(ii) **Death of Optionee.** In the event of the death of Optionee (a) during the term of this Option and while an Employee or Consultant of the Company and having been in Continuous Service Status since the date of grant of the Option, or (b) within

three months after Optionee's Termination Date, the Option may be exercised at any time within six months following the date of death by Optionee's estate or by a person who acquired the right to exercise the Option by bequest or inheritance, but only to the extent Optionee was vested in the Option as of the Termination Date.

6. **Non-Transferability of Option.** This Option may not be transferred in any manner otherwise than by will or by the laws of descent or distribution and may be exercised during the lifetime of Optionee only by him or her. The terms of this Option shall be binding upon the executors, administrators, heirs, successors and assigns of Optionee.

7. **Effect of Agreement.** Optionee acknowledges receipt of a copy of the Plan and represents that he or she is familiar with the terms and provisions thereof (and has had an opportunity to consult counsel regarding the Option terms), and hereby accepts this Option and agrees to be bound by its contractual terms as set forth herein and in the Plan. Optionee hereby agrees to accept as binding, conclusive and final all decisions and interpretations of the Plan Administrator regarding any questions relating to the Option. In the event of a conflict between the terms and provisions of the Plan and the terms and provisions of the Notice and this Agreement, the Plan terms and provisions shall prevail. The Option, including the Plan, constitutes the entire agreement between Optionee and the Company on the subject matter hereof and supersedes all proposals, written or oral, and all other communications between the parties relating to such subject matter.

6

[\(Back To Top\)](#)

## Section 5: EX-31.01 (SECTION 302 CEO CERTIFICATION)

Exhibit 31.01

### Certification of Principal Executive Officer Pursuant to Section 302 of Sarbanes-Oxley Act of 2002

I, Joseph Kennedy, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Pandora Media, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report, based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

June 1, 2012

/s/ Joseph Kennedy

Name: Joseph Kennedy  
Title: Chief Executive Officer, President and  
Chairman of the Board (Principal Executive  
Officer)

## Section 6: EX-31.02 (SECTION 302 CFO CERTIFICATION)

Exhibit 31.02

### Certification of Principal Financial Officer Pursuant to Section 302 of Sarbanes-Oxley Act of 2002

I, Steven Cakebread, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Pandora Media, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report, based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

June 1, 2012

/s/ Steven Cakebread

Name: Steven Cakebread

Title: *Executive Vice President and Chief Financial Officer (Principal Financial Officer)*

## Section 7: EX-32.01 (SECTION 906 CEO AND CFO CERTIFICATION)

Exhibit 32.01

### CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER AND PRINCIPAL FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF SARBANES-OXLEY ACT OF 2002

The certification set forth below is being submitted in connection with this Quarterly Report on Form 10-Q for the quarter ended April 30, 2012 (the "Report") for the purpose of complying with Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 (the "Exchange Act") and Section 1350 of Chapter 63 of Title 18 of the United States Code.

Each of the undersigned certifies that, to his knowledge:

1. the Report fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations

June 1, 2012

/s/ Joseph Kennedy

Name: Joseph Kennedy

Title: *Chief Executive Officer, President and Chairman  
of the Board (Principal Executive Officer)*

/s/ Steven Cakebread

Name: Steven Cakebread

Title: *Executive Vice President and Chief Financial  
Officer (Principal Financial Officer)*

This certification accompanying the Report is not deemed filed with the Securities and Exchange Commission for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liabilities such Section, and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before, on or after the date of the Report), irrespective of any general incorporation language contained in such filing.

[\(Back To Top\)](#)