STAMPS.COM INC
Form 10-Q
August 09, 2006

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2006

OR

o 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: 000-26427

Stamps.com Inc.
(Exact name of registrant as specified in its charter)

Delaware	77-0454966
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

12959 Coral Tree Place
Los Angeles, California 90066
(Address of Principal Executive Offices)

Registrant's telephone number, including area code: **(310) 482-5800**

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 þ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨ Accelerated filer þ Non-accelerated filer ¨

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

As of July 31, 2006, there were approximately 23,996,899 shares of the Registrant’s Common Stock issued and outstanding.

STAMPS.COM INC.

FORM 10-Q QUARTERLY REPORT FOR THE QUARTER ENDED JUNE 30, 2006

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

STAMPS.COM INC.
BALANCE SHEETS
(In thousands, except per share data)

	June 30, 2006 (unaudited)	December 31, 2005
Assets		
Current assets:		
Cash and cash equivalents	$ 18,838	$ 20,768
Restricted cash	554	554
Short-term investments	15,557	19,450
Trade accounts receivable, net	2,335	2,131
Other accounts receivable	257	628
Other current assets	2,209	1,278
Total current assets	39,750	44,809
Property and equipment, net	5,384	4,492
Intangible assets, net	3,116	3,666
Long-term investments	82,456	63,207
Other assets	3,596	2,280
Total assets	$ 134,302	$ 118,454
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 8,920	$ 8,514
Total current liabilities	8,920	8,514
Commitments and contingencies		
Stockholders' equity:		
Common stock, $.001 par value		
Authorized shares 47,500 in 2006 and 2005		
Issued shares of 23,963 in 2006 and 23,372 in 2005		
Outstanding shares of 23,654 in 2006 and 23,063 in 2005	47	46
Additional paid-in capital	616,357	607,869
Accumulated deficit	(486,166)	(493,683)
Treasury Stock, at cost, 309 shares in 2006 and 2005	(3,737)	(3,737)
Accumulated other comprehensive loss	(1,119)	(555)
Total stockholders' equity	125,382	109,940
Total liabilities and stockholders' equity	$ 134,302	$ 118,454

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

STAMPS.COM INC.
STATEMENTS OF INCOME
(In thousands, except per share data)
(Unaudited)

	Three Months ended June 30, 2006	Three Months ended June 30, 2005	Six Months ended June 30, 2006	Six Months ended June 30, 2005
Revenues:				
Service	$ 13,628	$ 10,439	$ 27,085	$ 19,539
PhotoStamps	3,747	1,159	7,607	1,159
Product	1,980	1,826	4,373	3,710
Other	805	799	1,637	1,612
Total revenues	20,160	14,223	40,702	26,020
Cost of revenues:				
Service	2,353	2,543	4,940	5,028
PhotoStamps	2,378	764	4,799	764
Product	628	545	1,381	1,071
Other	169	131	339	264
Total cost of revenues	5,528	3,983	11,459	7,127
Gross profit	14,632	10,240	29,243	18,893
Operating expenses:				
Sales and marketing	6,446	4,439	13,270	8,139
Research and development	2,159	1,571	4,498	3,076
General and administrative	3,213	2,512	6,371	4,897
Total operating expenses	11,818	8,522	24,139	16,112
Income from operations	2,814	1,718	5,104	2,781
Other income:				
Interest income	1,399	446	2,478	997
Other income	—	—	—	64
Total other income	1,399	446	2,478	1,061
Income before income taxes	4,213	2,164	7,582	3,842
Provision for income taxes Basic	53	43	65	80
Net income	$ 4,160	$ 2,121	$ 7,517	$ 3,762
Net income per share (see Note 3):				
Basic Basic	$ 0.18	$ 0.09	$ 0.32	$ 0.17
Diluted	$ 0.17	$ 0.09	$ 0.31	$ 0.16
Weighted average shares outstanding				
Basic Basic	23,601	22,689	23,435	22,602
Diluted	24,561	23,819	24,474	23,631

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

STAMPS.COM INC.
STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months ended June 31, 2006	Six Months ended June 31, 2005
Operating activities:		
Net income	$ 7,517	$ 3,762
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,408	1,488
Stock-based compensation expense	1,491	—
Changes in operating assets and liabilities:		
Trade accounts receivable	(204)	(355)
Other accounts receivable	371	170
Other assets	(1,316)	(705)
Prepaid expenses	(931)	(662)
Accounts payable and accrued expenses	405	1,018
Net cash provided by operating activities	8,741	4,716
Investing activities:		
Sale of short-term investments	22,146	4,877
Purchase of short-term investments	(18,211)	(6,373)
Sale of long-term investments	12,180	37,197
Purchase of long-term investments	(32,034)	(40,394)
Acquisition of property and equipment	(1,750)	(1,884)
Net cash used in investing activities	(17,669)	(6,577)
Financing activities:		
Proceeds from exercise of stock options	6,760	2,182
Issuance of common stock under ESPP	238	160
Net cash provided by financing activities	6,998	2,342
Net (decrease) increase in cash and cash equivalents	(1,930)	481
Cash and cash equivalents at beginning of period	20,768	11,198
Cash and cash equivalents at end of period	$ 18,838	$ 11,679

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

STAMPS.COM
NOTES TO FINANCIAL STATEMENTS
(ALL INFORMATION WITH RESPECT TO JUNE 30, 2006 AND 2005 IS UNAUDITED)

1. Summary of Significant Accounting Policies

Basis of Presentation

The financial statements included herein have been prepared by Stamps.com Inc. (Stamps.com or Company) without audit pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with US generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. The Company believes that the disclosures are adequate to make the information presented not misleading. It is suggested that these financial statements be read in conjunction with the financial statements and the notes thereto included in the Company's latest annual report on Form 10-K.

In the opinion of the Company, these unaudited financial statements contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly the financial position of the Company as of June 30, 2006, the results of its operations for the three months and six months ended June 30, 2006 and 2005, and its cash flows for the six months ended June 30, 2006 and 2005.

Use of Estimates and Risk Management

The preparation of financial statements in conformity with US generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates and such differences may be material to the financial statements. Examples include estimates of loss contingencies, promotional coupon redemptions and estimates regarding the useful lives of patents and other amortizable intangibles.

The Company is involved in various litigation matters as a claimant and a defendant. The Company records any amounts recovered in these matters when received. The Company records liabilities for claims against it when the loss is probable and estimable. Amounts recorded are based on reviews by outside counsel, in-house counsel and management. Actual results could differ from estimates.

Income Taxes

The provision for income taxes consists solely of alternative minimum federal and state taxes. The Company’s effective income tax rate differs from the statutory income tax rate primarily as a result of the establishment of a valuation allowance for the future benefits to be received from the deferred tax assets including net operating loss carryforwards and research tax credits carryforwards as well as the use of net operating losses to offset taxable income. The Company recorded a tax provision subject to the corporate alternative minimum federal and state taxes of approximately $53,000 and $43,000 for the three months ended June 30, 2006 and 2005, respectively, and $65,000 and $80,000 for the six months ended June 30, 2006 and 2005, respectively.

2. Legal Proceedings

Please refer to "Part II - Other Information - Item 1 - Legal Proceedings" of this report for a discussion of legal proceedings.

3. Net Income per Share

Net income per share represents net income attributable to common stockholders divided by the weighted average number of common shares outstanding during a reported period. The diluted net income per share reflects the potential dilution that could occur if securities or other contracts to issue common stock, including convertible preferred stock and stock options and warrants (commonly and hereafter referred to as "common stock equivalents"), were exercised or converted into common stock. Diluted net income per share is calculated by dividing net income during a reported period by the sum of the weighted average number of common shares outstanding plus common stock equivalents for the period. Basic and diluted income per share for the three and six months ended June 30, 2005 were calculated based on net income not including stock based compensation expense as required by Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" (SFAS 123R). The Company adopted SFAS 123R on January 1, 2006 using the modified prospective transition method which does not require the Company's prior period financial statements to be restated. Therefore, prior period earnings per share have not been restated as allowed by SFAS 123R. The following table reconciles share amounts utilized to calculate basic and diluted net income per share (in thousands, except per share data):

STAMPS.COM
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(ALL INFORMATION WITH RESPECT TO JUNE 30, 2006 AND 2005 IS UNAUDITED)

	Three Months Ended June 30,				Six Months Ended June 30,			
	2006		2005		2006		2005	
Net income	$	4,160	$	2,121	$	7,517	$	3,762
Basic - weighted average common shares		23,601		22,689		23,435		22,602
Diluted effect of common stock equivalents		960		1,130		1,039		1,029
Diluted - weighted average common shares		24,561		23,819		24,474		23,631
Earnings per share:								
Basic	$	0.18	$	0.09	$	0.32	$	0.17
Diluted	$	0.17	$	0.09	$	0.31	$	0.16

The calculation of dilutive shares excludes the effect of the following options that are considered anti-dilutive (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Anti-dilutive stock options shares	286	251	234	759

4. Stock-Based Employee Compensation

Effective January 1, 2006, the Company adopted the Statement of Financial Accounting Standards No. 123 (revised 2004), “Share-Based Payment” (SFAS 123R), and related SEC rules included in Staff Accounting Bulletin No. 107 (SAB 107), which require the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors including employee stock options and employee stock purchases related to the Employee Stock Purchase Plan (employee stock purchases) based on estimated fair values.

The Company adopted SFAS 123R using the modified prospective transition method, which requires the application of the accounting standard as of January 1, 2006, the first day of the Company’s fiscal year 2006. The Company’s Financial Statements as of and for the three and six months ended June 30, 2006 reflect the impact of SFAS 123R. In accordance with the modified prospective transition method, the Company’s Financial Statements for prior periods have not been restated to reflect, and do not include, the impact of SFAS 123R. Stock-based compensation expense recognized under SFAS 123R was $696,000 for the three months ended June 30, 2006 and $1.5 million for the six months ended June 30, 2006, which consist of stock-based compensation expense related to employee and director stock options and employee stock purchases of $696,000 and $0, respectively, for the three months ended June 30, 2006, and $992,000 and $499,000, respectively, for the six months ended June 30, 2006.

SFAS 123R requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in the Company’s Statement of Income. Prior to the adoption of SFAS 123R, the Company accounted for stock-based awards to employees and directors using the intrinsic value method in accordance with APB 25 as allowed under Statement of Financial Accounting Standards No. 123, “Accounting for

Stock-Based Compensation" (SFAS 123). Under the intrinsic value method, no stock-based compensation expense had been recognized in the Company's Statement of Income prior to January 1, 2006 because the exercise price of the Company's stock options granted to employees and directors was equal to or greater than the fair market value of the underlying stock at the date of grant.

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The following table illustrates the reported and pro forma effect on net income and earnings per share if the Company had elected to apply the fair value recognition provisions of SFAS 123 for the three and six months ended June 30, 2005 (in thousands, except per share data):

	Three Months Ended June 30, 2005		Six Months Ended June 30, 2005	
Net income as reported	$	2,121	$	3,762
Add: Stock price based employee expense included in net loss		—		—
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects		(274)		(602)
Net income pro forma	$	1,847	$	3,160
Basic net income per common share-as reported	$	0.09	$	0.17
Diluted net income per common share-as reported	$	0.09	$	0.16
Basic net income per common share-pro forma	$	0.08	$	0.14
Diluted net income per common share-pro forma	$	0.08	$	0.13

Stock-based compensation expense recognized during the period is based on the value of the portion of share-based payment awards that is ultimately expected to vest during the period. Stock-based compensation expense recognized in the Company's Statement of Income for the three and six months ended June 30, 2006 included 1) compensation expense for share-based payment awards granted prior to, but not yet vested as of January 1, 2006 based on the grant date fair value estimated in accordance with the pro forma provisions of SFAS 123 and 2) compensation expense for the share-based payment awards granted subsequent to December 31, 2005 based on the grant date fair value estimated in accordance with the provisions of SFAS 123R.

Compensation expense recognized for all employee stock options awards granted is recognized using the straight-line single method over their respective vesting periods of three or four years. As stock-based compensation expense recognized in the Statement of Income for the three and six months ended June 30, 2006 is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. In the Company's pro forma information required under SFAS 123 for the periods prior to fiscal 2006, the Company accounted for forfeitures as they occurred.

SFAS 123R requires the cash flow resulting from tax benefits resulting from tax deduction in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. Prior to fiscal 2005 the Company had a history of net operating losses and because it is uncertain as to when and if it may realize its deferred tax assets, the Company has placed a valuation allowance against its otherwise recognizable deferred tax asset. Therefore, there are no excess tax benefits recorded in the financing cash inflow that would have been classified as an operating cash inflow if the Company had not adopted SFAS 123R. During the three and six months ended June 30, 2006, the Company received $1.7 million and $7.0 million, respectively, in cash from stock options exercised and from shares issued through the Employee Stock Purchase Program.

Upon adoption of SFAS 123R the Company continued to use the Black-Scholes option valuation model, which requires management to make certain assumptions for estimating the fair value of employee stock options granted at the date of the grant. The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimates, in management's opinion the existing models may not necessarily provide a reliable single measure of the fair value of the Company's employee stock options. Although the fair value of employee stock options is determined in accordance with SFAS 123R using an option valuation model, that value may not be indicative of the fair value observed in a willing buyer/willing seller market transaction.

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For options granted, the Company's assumption of expected volatility for valuing options using the Black-Scholes model was based on the historical volatility of the Company's stock price for the period January 1, 2002 through the date of option grant because management believes the historical volatility since January 1, 2002 is more representative of prospective volatility. The risk-free interest rate is based on U.S. Treasury zero-coupon issues with a remaining term equal to the expected life assumed at the date of grant.

The following are the weighted average assumptions used in the Black-Scholes valuation model for the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Expected dividend yield	—	—	—	—
Risk-free interest rate	5.0%	4.01%	4.78%	3.84%
Expected volatility	49%	48%	49%	48%
Expected life (in years)	5	5	5	5
Expected forfeiture rate	16%	—	14%	—

The following table summarizes stock option activity related to the Company's plan for the six months ended June 30, 2006:

	Number of Stock Options (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2005	2,608	$ 15.03		
Granted	202	31.89		
Exercised	(567)	11.97		
Forfeited or expired	(33)	25.26		
Balance at June 30, 2006	2,210	16.45	6.5	$ 23,096
Exercisable at June 30, 2006	1,754	15.92	6.2	$ 20,883

The weighted average grant date fair value of options granted during the six months ended June 30, 2006 and 2005 was $15.51 and $7.46, respectively. The total intrinsic value of options exercised during the six months ended June 30, 2006 and 2005 was $8,633,927 and $3,457,428, respectively.

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(ALL INFORMATION WITH RESPECT TO JUNE 30, 2006 AND 2005 IS UNAUDITED)

The following table summarizes the status of the Company's nonvested shares as of June 30, 2006:

	Number of Stock Options (in thousands)	Weighted Average Grant Date Fair Value
Nonvested at December 31, 2005	416	$ 7.37
Granted	202	15.51
Vested	(81)	6.26
Forfeited	(33)	14.11
Nonvested at June 30, 2006	504	10.91

As of June 30, 2006, there was approximately $4.7 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements, which is expected to be recognized over a weighted-average period of 7.8 years.

5. Goodwill and Intangible Assets

The Company wrote off all of its goodwill in the first quarter of 2001 due to impairment. The Company's other intangible assets, which consist of patents, trademarks and other intellectual property with a gross carrying value of $8.9 million as of June 30, 2006 and December 31, 2005 and accumulated amortization of approximately $5.8 million and $5.2 million as of June 30, 2006 and December 31, 2005, respectively, continue to be amortized over their expected useful lives ranging from 4 to 17 years with a remaining weighted average amortization period of 1.6 years.

Aggregate amortization expense on intangible assets was approximately $275,000 for the three months ended June 30, 2006 and 2005, respectively and $550,000 for the six months ended June 30, 2006 and 2005, respectively.

6. Comprehensive Income

The following table provides the data required to calculate comprehensive income (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Net income	$ 4,160	$ 2,121	$ 7,517	$ 3,762
Unrealized income (loss) on investments	(423)	393	(564)	68
Comprehensive income	$ 3,737	$ 2,514	$ 6,953	$ 3,830

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements relate to expectations concerning matters that are not historical facts. Words such as "projects," "believes," "anticipates," "estimates," "plans," "expects," "intends," and similar words and expressions are intended to identify forward-looking statements. Although Stamps.com believes that such forward-looking statements are reasonable, we cannot assure you that such expectations will prove to be correct. Factors that could cause actual results to differ materially from such expectations are disclosed herein. All forward-looking statements attributable to Stamps.com are expressly qualified in their entirety by such language. Stamps.com does not undertake any obligation to update any forward-looking statements. You are also urged to carefully review and consider the various disclosures we have made which describe certain factors which affect our business. The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our financial statements and the related notes thereto.

Stamps.com, NetStamps, PhotoStamps, Hidden Postage, Stamps.com Internet postage and the Stamps.com logo are our trademarks. This report also includes trademarks of entities other than Stamps.com.

Overview

Stamps.comÒ (the "Company" or "Stamps.com") is the leading provider of Internet-based postage solutions. Our core service allows customers to buy and print United States Postal Service ("US Postal Service" or "USPS") approved postage using any PC, an ordinary inkjet or laser printer, and an Internet connection. Customers use our service to mail and ship a variety of mail pieces including postcards, envelopes, flats and packages, and using a wide range of USPS mail classes including First Class Mail®, Priority Mail®, Express Mail®, Media Mail®, Parcel Post®, and others. Our customers include home businesses, small businesses, corporations and individuals. In 1999, we became the first ever USPS-licensed vendor to offer PC Postage® in a software-only business model. On August 10, 2004, we publicly launched a market test of PhotoStamps®, a new form of postage that allows consumers to turn digital photos, designs or images into valid US postage. We completed the first market test on September 30, 2004, launched a second market test of PhotoStamps on May 17, 2005, and subsequently a third market test on May 17, 2006. This third phase of the market test has an initial authorization period of one year, through May 16, 2007, and includes an option for the US Postal Service to extend the test for a second year to May 16, 2008. Throughout this document and in general when we refer to our core business, we mean the PC Postage business which excludes only the PhotoStamps business.

Stamps.com Inc. was founded in September 1996 to investigate the feasibility of entering into the US Postal Service's Information-Based Indicia Program and to initiate the certification process for our PC Postage service. In January 1998, we were incorporated in Delaware as StampMaster, Inc. and we changed our name to Stamps.com Inc. in December 1998. We completed our initial public offering in June 1999, and our common stock is listed on the Nasdaq stock market under the symbol "STMP."

Our principal executive offices are located at 12959 Coral Tree Place, Los Angeles, California, 90066, and our telephone number is (310) 482-5800.

Our Services and Products

We offer the following products and services to our customers:

PC Postage Service

Our USPS-approved PC Postage service enables users to print information-based indicia, or electronic stamps, directly onto envelopes, plain paper, or labels using ordinary laser or inkjet printers. Our service currently supports USPS classes including First-Class MailÒ, Priority MailÒ, Express MailÒ, Parcel Post®, Media MailÔ and Bound Printed Matter. Customers can also add USPS Special Services such as Delivery Confirmation™, Signature Confirmation™, Registered Mail, Certified Mail, Insured Mail, Return Receipt, Collect on Delivery and Restricted Delivery to their mail pieces. Our service requires only a standard PC, printer and Internet connection. Our free software can be downloaded from the Internet or installed from a CD-ROM. After installing the software and completing a registration process, customers can purchase and print postage 24 hours a day, seven days a week. When a customer purchases postage for use through our service, the customer pays face value, and the funds are transferred directly from the customer's account to the US Postal Service's account. The majority of new customers currently signing up for our service pay a monthly convenience fee of $15.99. Our current customer mix includes monthly convenience fees ranging from $4.49 to $24.99 or more based on individual pricing and promotions.

Stamps.com offers its customers three primary ways to print PC Postage. First, our NetStamps® feature enables customers to print postage for any value or any class of mail or package on NetStamps labels. After they are printed, NetStamps can be used just like regular stamps. Second, our shipping feature tab allows customers to print postage for packages on plain 8.5” x 11” paper or on special labels, and to add electronic Delivery or Signature Confirmation at discounted prices. Third, our mailing feature tab is typically used to print the postage and address directly on envelopes or on other types of mail or labels, in a single-step process that saves time and provides a professional look. Our PC Postage services also incorporate address verification technology that verifies each destination address for mail sent using our service against a database of all known addresses in the U.S. In addition, our PC Postage services have been designed to integrate into common small business and productivity software applications such as word processing, contact and address management, and accounting and financial applications.

PhotoStamps®

On May 17, 2005, we publicly launched our second market test of PhotoStamps, a patented form of postage that allows consumers to turn digital photos, designs or images into valid U.S. postage. PhotoStamps is used as regular postage to send letters, postcards or packages. On May 17, 2006 we launched a new PhotoStamps feature that allows businesses to use PhotoStamps to create awareness for their products or services, to build their brand, or for other commercial applications. Customers of PhotoStamps upload a digital photograph or image file, customize the look and feel by choosing one of ten different border colors to compliment the photos, select the value of postage, and place the order online. Each sheet includes 20 individual PhotoStamps, and orders arrive via US Mail in a few business days. In addition to the sheet format, PhotoStamps are also available in a roll form factor for use in higher volume applications. Individual rolls are available in custom lengths ranging from 250 to 10,000 PhotoStamps, and in denominations ranging from $0.24 for postcard rates to $4.05 for one pound packages. The product is available via our website at www.photostamps.com. PhotoStamps is currently offered for $17.99 for a single sheet of $.39 value PhotoStamps. Pricing may vary depending upon the postage denomination, volume of PhotoStamps purchased and promotions.

Since the beginning of the second market test, PhotoStamps has been prominently featured in the national media. For example, in its December 19, 2005 issue, BusinessWeek named PhotoStamps one of its Best Products for 2005. From May 2005 to June 2006, we shipped approximately 950,000 PhotoStamps sheets, or approximately 19 million individual PhotoStamps. We are currently authorized to sell PhotoStamps under the third phase market test that began May 17, 2006 and continues through May 16, 2007, with an option for the US Postal Service to extend the test for a second year to May 16, 2008.

Supplies Store

With the launch of NetStamps in July 2002, we began selling NetStamps labels directly to our customers via our Supplies Store (previously also referred to as our “Online Store”) which is accessible to our customers from within our PC Postage software. Our Supplies Store has since expanded to sell themed NetStamps labels, shipping labels, other mailing labels, dedicated postage printers, OEM and private label inkjet and laser toner cartridges, scales, and other mailing and shipping-focused office supplies. We plan to continue to increase the breadth of products offered in our Supplies Store in order to provide a more complete service to our customers, and with the goal of increasing our revenue.

Branded Insurance

We offer Stamps.com branded insurance to our users so that they may insure their mail or packages in a fully integrated, online process that eliminates any trips to the Post Office or the need to complete any special forms (we also offer official US Postal Service insurance alongside our branded insurance product). Our Stamps.com branded insurance is currently offered at a ten percent discount to the rates offered by the U.S. Postal Service. As insurance is purchased by our customers, we pass along the necessary information to the insurance provider. Our branded insurance program is currently provided in partnership with the broker Parcel Insurance Plan and is underwritten by Fireman's Fund.

Recent Developments

On July 25, 2006, we released a new software platform that allows us to provide a single web presentation and e-commerce system for all Stamps.com products and services. The new system will, among other things, provide enhanced cross-selling and up-selling tools, automated marketing, and item cataloging and display. This new system will also serve as the foundation for our future e-commerce initiatives.

On July 25, 2006, we also announced plans to release version 6.0 of our PC Postage client software into beta. This updated client software is built to take full advantage of our new software platform. Version 6.0 also includes new features such as an international shipping capability with fully integrated customs forms. We expect to move version 6.0 into general release during the third quarter of 2006.

Critical Accounting Policies

General. The discussion and analysis of our financial condition and results of operations are based on our Company's financial statements which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to patents, contingencies and litigation. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our financial statements.

Revenue Recognition. We recognize revenue from product sales or services rendered, as well as from licensing the use of our software and intellectual property, when the following four revenue recognition criteria are met: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the selling price is fixed or determinable, and collectibility is reasonably assured.

Service revenue is based on monthly convenience fees and is recognized in the period that services are provided. Product sales, net of return allowances, are recorded when the products are shipped and title passes to customers. Items, including PhotoStamps, sold to customers are made pursuant to a sales contract that provides for transfer of both title and risk of loss upon our delivery to the carrier. Return allowances, which reduce product revenue by our best estimate of expected product returns, are estimated using historical experience. Licensing revenue is recognized ratably over the contract period. Commissions from the advertising or sale of products by a third party vendor to our customer base are recognized when the revenue is earned and collection is deemed probable.

Customers who purchase postage for use through our NetStamps, shipping label or mailing features, pay face value, and the funds are transferred directly from the customers to the US Postal Service. No revenue is recognized for this postage as it is purchased by our customers directly from the US Postal Service.

PhotoStamps revenue includes the price of postage and is made pursuant to a sales contract that provides for transfer of both title and risk of loss upon our delivery to the carrier.

On a limited basis, we allow third parties to offer products and promotions to the Stamps.com customer base. These arrangements generally provide payment in the form of a flat fee or revenue sharing arrangements where we receive payment upon customers accessing third party products and services. Total revenue from such advertising arrangements is currently immaterial.

We provide our customers with the opportunity to purchase parcel insurance directly through the Stamps.com software. Insurance revenue represents the gross amount charged to the customer for purchasing insurance and the related cost represents the amount paid to the insurance broker, Parcel Insurance Plan. We recognize revenue on insurance purchases upon the ship date of the insured package.

Licensing revenue for the use of our software and intellectual property is recognized when the following four revenue recognition criteria are met: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the selling price is fixed or determinable, and collectibility is reasonably assured.

Advertising Costs. We expense the costs of producing advertisements as incurred, and expense the costs of communicating and placing the advertising in the period in which the advertising space or airtime is used.

Internet Advertising. We recognize expense based on the specifics of the individual agreements. Under partner and affiliate agreements, third parties refer prospects to our web site and we pay the third parties when the customer completes the customer registration process, completes the first purchase or in some cases, upon the first successful billing of a customer. We record these expenses on a monthly basis as prospects are successfully converted to customers.

Intangibles. We make an assessment of the estimated useful lives of our patents and other amortizable intangibles. These estimates are made using various assumptions that are subjective in nature and could change as economic and competitive conditions change. If events were to occur that would cause our assumptions to change, the amounts recorded as amortization would be adjusted.

Contingencies and Litigation. We are involved in various litigation matters as a claimant and as a defendant. We record any amounts recovered in these matters when collection is certain. We record liabilities for claims against us when the losses are probable and estimatable. Any amounts recorded would be based on reviews by outside counsel, in-house counsel and management. Actual results may differ from estimates.

Promotional Expense. New core service customers are generally offered promotional items that are redeemed using coupons that are qualified for redemption after a customer is successfully billed beyond an initial trial period. This includes free postage and a free digital scale and is expensed in the period in which a customer qualifies using estimated redemption rates based on historical data. Promotional expense which is included in cost of service is incurred as customers qualify and thereby may not correlate directly with changes in revenue as the revenue associated with the acquired customer is earned over the customer's lifetime.

Section 382 Update

Under Internal Revenue Code Section 382, a change in ownership can occur whenever there is a shift in ownership by more than 50 percentage points by one or more five-percent shareholders within a three-year period. When a change of ownership is triggered, our net operating loss ("NOL" or "NOLs") asset may be impaired. We estimate that, as of March 31, 2006 we are approximately at 25% compared with the 50% level that would trigger impairment of our NOL asset. As part of our ongoing program to preserve future use of our NOL assets, *Stamps.com requests that all of our current stockholders and prospective investors contact us prior to allowing their ownership interest to reach a five-percent level.*

Results of Operations

During the second quarter of 2006, we experienced continued revenue growth in our core PC Postage business and PhotoStamps sales continued to be strong despite the expected second quarter seasonal slowdown. Our total revenue during the second quarter of 2006 was $20.2 million, compared to $14.2 million during the comparable period in 2005. Total postage printed using our service during the second quarter of 2006 was up 22% compared to the second quarter of 2005. Gross customer core business acquisition was approximately 87,000 during the second quarter of 2006, up from approximately 66,000 during the second quarter of 2005.

The following table sets forth our results of operation as a percentage of total revenue for the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Total Revenues				
Service	68%	73%	66%	75%
PhotoStamps	19%	8%	19%	5%
Products	9%	13%	11%	14%
Other	4%	6%	4%	6%
Total revenues	100%	100%	100%	100%
Cost of revenues				
Service	11%	18%	12%	19%
PhotoStamps	12%	5%	12%	3%
Products	3%	4%	3%	4%
Other	1%	1%	1%	1%
Total cost of revenues	27%	28%	28%	27%
Gross profit	73%	72%	72%	73%
Operating expenses:				
Sales and marketing	32%	31%	32%	31%
Research and development	11%	11%	11%	12%
General and administrative	16%	18%	16%	19%
Total operating expenses	59%	60%	59%	62%
Income (loss) from operations	14%	12%	13%	11%
Other income (expense), net	7%	3%	6%	4%
Income (loss) before income taxes	21%	15%	19%	15%
Provision for income taxes	0%	0%	0%	0%
Net income (loss)	21%	15%	19%	15%

Revenue. Revenue was derived primarily from four sources: (1) service fees charged to customers for use of our PC Postage service; (2) PhotoStamps revenue from the sale of PhotoStamps; (3) product sales consisting of Supplies Store revenue from the direct sale of consumables and supplies; and (4) other revenue consisting of advertising revenue from controlled access advertising to our existing customer base, insurance revenue from our branded insurance offering, and licensing revenue. Revenue increased from $14.2 million in second quarter 2005 to $20.2 million in second quarter 2006, an increase of 42%. Revenue increased from $26.0 million during the six months ended June 30, 2005 to $40.7 million during the six months ended June 30, 2006, an increase of 56%.

Service fee revenue increased from $10.4 million in the second quarter of 2005 to $13.6 million in the second quarter of 2006, an increase of 31%. Service fee revenue increased from $19.5 million during the six months ended June 30, 2005 to $27.1 million during the six months ended June 30, 2006, an increase of 39%. The increase in service fee revenue is primarily due to the growth of our customer base and the migration of our existing customers from our Simple Plan price point of $4.49 per month to the Power/Pro Plan at $15.99 per month and the Premier Plan at higher price points, resulting in higher service fee revenue per customer. We successfully billed approximately 324,000 and 327,000 unique customers during the first and second quarters of 2006, respectively, as compared to approximately 291,000 and 300,000 unique customers during the first and second quarters of 2005, respectively. Average service fee revenue per successfully billed customer was approximately $42 during the second quarter of 2006 as compared to $35 in the second quarter of 2005. As a percentage of total revenue, service fee revenue decreased five percentage points and nine percentage points during the three and six months ended June 30, 2006, respectively, as compared to the three and six months ended June 30, 2005. The decrease in service fee revenue as a percentage of total revenue is attributable to the increase in revenue from our PhotoStamps product. As a percentage of revenue, service fee revenue may decline over future periods as we continue to sell PhotoStamps under our current market test period which began on May 17, 2006.

PhotoStamps revenue increased from $1.2 million in the second quarter of 2005 to $3.7 million in the second quarter of 2006, an increase of 223%. PhotoStamps revenue increased from $1.2 million during the six months ended June 30, 2005 to $7.6 million during the six months ended June 30, 2006, an increase of 556%. As a percentage of total revenue, PhotoStamps revenue increased 11 percentage points and 14 percentage points during the three and six months ended June 30, 2006, respectively, as compared to the three and six months ended June 30, 2005. The increase, both on an absolute basis and as a percentage of total revenue is primarily due to the increase in customer orders as a result of our marketing efforts. We had no PhotoStamps revenue during the first quarter of 2005 as the second market test had not yet been launched. We expect PhotoStamps revenue to grow both on an absolute basis and as a percentage of total revenue in future periods as we expand our sales during our current market test period.

Product revenue increased from $1.8 million in the second quarter of 2005 to $2.0 million in the second quarter of 2006, an increase of eight percent. Product revenue increased from $3.7 million during the six months ended June 30, 2005 to $4.4 million during the six months ended June 30, 2006, an increase of 18%. The increase is primarily due to the expansion of our consumable and supplies sales through our Supplies Store as a result of our continued effort to market these offerings to our existing and new customers. As a percentage of total revenue, product revenue decreased four percentage points and three percentage points during the three and six months ended June 30, 2006, respectively, as compared to the three and six months ended June 30, 2005. This decrease is primarily due to the increase in PhotoStamps revenue. We expect product revenue to continue to increase on an absolute basis as we add additional stock keeping units (SKUs) to our Supplies Store, and as we continue to market to our existing and new customers.

Other revenue increased from $800,000 in the second quarter of 2005 to $805,000 in the second quarter of 2006, an increase of one percent. Other revenue was $1.6 million in each of the six months ended June 30, 2005 and 2006. As a percentage of total revenue, other revenue decreased two percentage points during the three and six months ended June 30, 2006, as compared to the three and six months ended June 30, 2005. The decrease in other revenue as a percentage of total revenue is primarily due to the increase in PhotoStamps revenue. As a percentage of revenue, other revenue may decline over future periods as we continue to sell PhotoStamps under our current market test period. Included in other revenue is our branded insurance program which was approximately $346,000 and $724,000 for the three and six months ended June 30, 2006, respectively, or approximately two percent of total revenue.

Cost of Revenue. Cost of revenue principally consists of the cost of customer service, certain promotional expenses, system operating costs, credit card processing fees, the cost of postage for PhotoStamps, image review, printing and fulfillment costs for PhotoStamps, parcel insurance offering costs, customer misprints and products sold through our Supplies Store and the related costs of shipping and handling. Cost of revenue increased from $4.0 million in the second quarter of 2005 to $5.5 million in the second quarter of 2006, an increase of 39%. Cost of revenue increased from $7.1 million during the six months ended June 30, 2005 to $11.5 million during the six months ended June 30, 2006, an increase of 61%.The increase is primarily due to the increase in PhotoStamps cost of revenue as a result of the increase in customer orders due to our marketing efforts. As a percentage of total revenue, cost of revenue was 28% and 27% during the three months ended June 30, 2005 and 2006, respectively. As a percentage of total revenue, cost of revenue was 27% and 28% during the six months ended June 30, 2005 and 2006, respectively.

Cost of service revenue decreased from $2.5 million in the second quarter of 2005 to $2.4 million in the second quarter of 2006, a decrease of seven percent. This is primarily due to the decrease in promotional expense, offset by an increase in credit card fees. Cost of service revenue was $5.0 million during the six months ended 2005 and 2006, respectively. As a percentage of total revenue, cost of service revenue decreased seven percentage points during the three and six months ended June 30, 2006, respectively, as compared to the three and six months ended June 30, 2005. The decrease in cost of service revenue as a percentage of total revenue is primarily due to the increase in PhotoStamps revenue.

The decrease in promotional expense is attributable to the decrease in the redemption rate of our promotional offerings as well as a reduced carrying cost of promotional items. Promotional expenses are primarily incurred as customers qualify for the promotion and thereby may not correlate directly with changes in revenue. Promotional expense includes free postage and a free digital scale offered to new customers, and was approximately $570,000 and $750,000 in the second quarters of 2006 and 2005, respectively, and $1.3 million and $1.5 million during the six months ended June 30, 2006 and 2005, respectively. Promotional expense, which represents a material portion of total cost of service revenue, is expensed in the period in which a customer qualifies for the promotion. However, the revenue associated with the acquired customer is earned over the customer's lifetime. Therefore, promotional expense for newly acquired customers may be higher than the revenue earned from those customers in that period. The increase in credit card fees is a result of higher volume in credit card transactions for collecting subscription fees as a result of the increase in customer acquisitions due to marketing efforts.

Cost of PhotoStamps revenue increased from $764,000 in the second quarter of 2005 to $2.4 million in the second quarter of 2006, an increase of 211%. PhotoStamps revenue increased from $764,000 during the six months ended June 30, 2005 to $4.8 million during the six months ended June 30, 2006, an increase of 528%. As a percentage of total revenue, cost of PhotoStamps increased seven percentage points and nine percentage points during the three and six months ended June 30, 2006, respectively, as compared to the three and six months ended June 30, 2005. The increase, both on an absolute basis and as a percentage of total revenue is primarily due to the increase in customer orders as a result of marketing efforts. Additionally, the gross margin from PhotoStamps is significantly lower than that of our other sources of revenue because we include the stated value of US Postal Service postage as part of our cost of PhotoStamps revenue. As a result, future increases in PhotoStamps sales would further increase the overall cost of revenue as a percentage of total revenue. We had no PhotoStamps revenue during the first quarter of 2005 as the second market test had not yet been launched. We expect PhotoStamps revenue to grow both on an absolute basis and as a percentage of total revenue in future periods.

Cost of product revenue increased from $545,000 in the second quarter of 2005 to $628,000 in the second quarter of 2006, an increase of 15%. Cost of product revenue increased from $1.1 million during the six months ended June 30, 2005 to $1.4 million during the six months ended June 30, 2006, an increase of 29%. The increase is primarily due to the expansion of our consumable and supplies sales through our Supplies Store as a result of our continued effort to market these offerings to our existing and new customers. As a percentage of total revenue, cost of product revenue decreased one percentage point during each of the three and six months ended June 30, 2006, as compared to the three and six months ended June 30, 2005. We expect the cost of product sales to continue to increase in future periods which is consistent with the aforementioned expectation that product sales will also increase in future periods.

Cost of other revenue increased from $131,000 in the second quarter of 2005 to $169,000 in the second quarter of 2006, an increase of 29%. Cost of other revenue increased from $264,000 during the six months ended June 30, 2005 to $339,000 during the six months ended June 30, 2006, an increase of 28%. The increase is primarily due to the increase in insurance sales and other advertising revenue. As a percentage of total revenue, cost of other revenue was one percent during the three and six months ended June 30, 2006 and 2005, respectively.

Sales and Marketing. Sales and marketing expense principally consists of costs associated with strategic partnership relationships, advertising, and compensation and related expenses for personnel engaged in sales, marketing, and business development activities. Sales and marketing expense increased from $4.4 million in the second quarter of 2005 to $6.4 million in the second quarter of 2006, an increase of 45%. Sales and marketing expense increased from $8.1 million during the six months ended June 30, 2005 to $13.3 million during the six months ended June 30, 2006, an increase of 63%. The increase in sales and marketing expense is primarily due to the increase in various marketing program expenditures relating to the acquisition of customers for our core business and for PhotoStamps. Ongoing marketing programs include the following: traditional advertising, partnerships, customer referral programs, customer remarketing efforts, telemarketing, direct mail, and online advertising. Additionally, included in sales and marketing expense for the second quarter of 2006 and the six months ended June 30, 2006 were approximately $68,000 and $173,000, respectively, of stock-based employee compensation expense related to our adoption of the new accounting pronouncement effective on January 1, 2006. We did not incur a similar charge during the comparable periods of 2005. As a percentage of total revenue, sales and marketing expense increased one percentage point during each of the three and six months ended June 30, 2006, as compared to the three and six months ended June 30, 2005. We currently expect sales and marketing expenses to increase in fiscal 2006 as compared to fiscal 2005 as we increase our marketing activity and customer acquisition.

Research and Development. Research and development expense principally consists of compensation for personnel involved in the development of our services and expenditures for consulting services and third party software. Research and development expense increased from $1.6 million in the second quarter of 2005 to $2.2 million in the second quarter of 2006, an increase of 37%. Research and development expense increased from $3.1 million during the six months ended June 30, 2005 to $4.5 million during the six months ended June 30, 2006, an increase of 46%.

This increase is primarily due to the increase in salary, software maintenance, and depreciation expense. Additionally, included in research and development expense for the second quarter of 2006 and the six months ended June 30, 2006 were approximately $115,000 and $418,000, respectively, of stock-based employee compensation expense related to our adoption of the new accounting pronouncement effective on January 1, 2006. We did not incur a similar charge during the comparable periods of 2005. As a percentage of total revenue, research and development expense was 11% in the second quarter of each of 2006 and 2005. As a percentage of total revenue, research and development expense decreased one percentage point during the six months ended June 30, 2006 as compared to the six months ended June 30, 2005. We currently expect research and development expense to increase in fiscal 2006 as compared to fiscal 2005 as we expect to continue to increase our investment in our technology.

General and Administrative. General and administrative expense principally consist of compensation and related costs for executive and administrative personnel, fees for legal and other professional services, depreciation of equipment and software used for general corporate purposes and amortization of intangible assets. General and administrative expense increased from $2.5 million in the second quarter of 2005 to $3.2 million in the second quarter of 2006, an increase of 28%. General and administrative expense increased from $4.9 million during the six months ended June 30, 2005 to $6.4 million during the six months ended June 30, 2006, an increase of 30%. The increase in general and administrative expense is primarily due to the increase in legal fee and salary expense. Additionally, included in general and administrative expense for the second quarter of 2006 and the six months ended June 30, 2006 were approximately $470,000 and $738,000, respectively, of stock-based employee compensation expense related to our adoption of the new accounting pronouncement effective on January 1, 2006. We did not incur a similar charge during the comparable periods of 2005. As a percentage of total revenue, general and administrative expense decreased two percentage points and three percentage points during the three and six months ended June 30, 2006, respectively, as compared to the three and six months ended June 30, 2005. We currently expect general and administrative expenses to increase in fiscal 2006 as compared to fiscal 2005, but decrease as a percentage of total revenue.

Other Income, Net. Other income, net consists of interest income from cash equivalents and short-term and long-term investments. Other income, net increased from $446,000 in the second quarter of 2005 to $1.4 million in the second quarter of 2006, an increase of 214%. Other income, net increased from $1.1 million during the six months ended June 30, 2005 to $2.5 million during the six months ended June 30, 2006, an increase of 134%. As a percentage of total revenue, other income, net increased four percentage points and two percentage points during the three and six months ended June 30, 2006, respectively, as compared to the three and six months ended June 30, 2005. The increase, both on an absolute basis and as a percentage of total revenue is due to the increase in interest rates and invested balance as we maintain our profitability. We currently expect other income to increase in fiscal 2006 as compared to fiscal 2005 due to increased invested balances.

Liquidity and Capital Resources

As of June 30, 2006 and 2005 we had approximately $117 million and $92 million, respectively, in cash, restricted cash and short-term and long-term investments. We invest available funds in short and long-term money market funds, commercial paper, corporate notes and municipal securities and do not engage in hedging or speculative activities.

In November 2003, we entered into a facility lease agreement commencing in March 2004 for our new corporate headquarters with aggregate lease payments of approximately $4 million through February 2010.

The following table is a schedule of our contractual obligations and commercial commitments which is comprised of the future minimum lease payments under operating leases at June 30, 2006 (in thousands):

		Operating
Six months ending December 31, 2006	$	318
Years ending December 31:		
2007		694
2008		751
2009		794
2010		134
Thereafter		—
	$	2,691

Net cash provided by operating activities was $8.7 million and $4.7 million during the six months ended June 30, 2006 and 2005, respectively. The increase in net cash provided by operating activities resulted primarily from the increase in revenue and expanding gross margin and operating cash flow.

Net cash used in investing activities was $17.7 million and $6.6 million during the six months ended June 30, 2006 and 2005, respectively. The increase in net cash used in investing activities resulted primarily from the additional purchase of investments as a result of the Company's profitability.

Net cash provided by financing activities was $7.0 million and $2.3 million during the six months ended June 30, 2006 and 2005, respectively. The increase in net cash provided by financing activities resulted primarily from the exercise of stock options by our employees.

We believe our available cash and marketable securities, together with the cash flow from operations will be sufficient to fund our business for the foreseeable future.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our exposure to market rate risk for changes in interest rates relates primarily to our investment portfolio. We have not used derivative financial instruments in our investment portfolio. Our cash equivalents and investments are comprised of Money Market, U.S. government obligations and public corporate debt securities with weighted average maturities of 466 days at June 30, 2006. Our cash equivalents and investments, net of restricted cash, approximated $117 million and had a related weighted average interest rate of approximately 4.2%. Interest rate fluctuations impact the carrying value of the portfolio. We do not believe that the future market risks related to the above securities will have a material adverse impact on our financial position, results of operations or liquidity.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain a set of disclosure controls and procedures that are designed to ensure that information to be disclosed by us under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time period specified in the Securities and Exchange Commission's rules and forms. As of the end of the period covered by this report, we carried out an evaluation pursuant to Rules 13a-15(e) and 15d-15(e) of the Exchange Act, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective and adequate to ensure that material information and other information requiring disclosure is identified and communicated on a timely basis.

Changes in Internal Controls

There have been no changes in our internal controls over financial reporting or in other factors during the period covered by this report that has affected or could affect these controls subsequent to the date of their evaluation.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On October 22, 2004, Kara Technology Incorporated filed suit against us in the United States District Court for the Southern District of New York, alleging, among other claims, that Stamps.com infringed certain Kara Technology patents and that Stamps.com misappropriated trade secrets owned by Kara Technology, most particularly with respect to our NetStamps feature. Kara Technology seeks an injunction, unspecified damages, and attorneys' fees. On February 9, 2005, the court granted our motion to transfer this suit to the United States District Court for the Central District of California. The court has scheduled a "Markman" hearing to construe the terms of the Kara Technology patents for August 21, 2006, and has scheduled a trial commencement date of January 9, 2007. We dispute Kara Technology's claims and intend to defend the lawsuit vigorously.

On October 25, 2004, VCode Holdings, Inc. and VData LLC filed suit against Adidas Salomon AG in the United States District Court for the District of Minnesota, alleging infringement of U.S. Patent No. 5,612,524 ("the '524 patent"), which allegedly covers use of data matrices. The complaint sought an injunction, unspecified damages, and attorneys' fees. On or about December 30, 2004, the plaintiffs filed a First Amended Complaint against us, as well as Adidas Salomon AG, Adidas America, Inc., Advanced Micro Devices, Inc., Boston Scientific Corp. and Hitachi Global Storage Technologies (Thailand), Ltd., alleging infringement of the '524 patent. On July 25, 2005, the Court granted the plaintiffs' motion to file a Second Amended Complaint adding Hitachi Global Storage Technologies, Inc. as a defendant. Each of our co-defendants has settled for undisclosed terms. On April 19, 2006, Stamps.com and the plaintiffs settled. Under the terms of the settlement, Stamps.com paid the plaintiffs an immaterial amount of cash for a license to the patents involved in the lawsuit.

In May and June 2001, we were named, together with certain of our current and former board members and/or officers, as a defendant in 11 purported class-action lawsuits, filed in the United States District Court for the Southern District of New York. The lawsuits allege violations of the Securities Act of 1933 and the Securities Exchange Act of 1934 in connection with our initial public offering and secondary offering of our common stock. The lawsuits also name as defendants the principal underwriters in connection with our initial and secondary public offerings, including Goldman, Sachs & Co. (in some of the lawsuits sued as The Goldman Sachs Group Inc.) and BancBoston Robertson Stephens, Inc. The lawsuits allege that the underwriters engaged in improper commission practices and stock price manipulations in connection with the sale of our common stock. The lawsuits also allege that we and/or certain of our officers or directors knew of or recklessly disregarded these practices by the underwriter defendants, and failed to disclose them in our public filings. Plaintiffs seek damages and statutory compensation, including prejudgment and post-judgment interest, costs and expenses (including attorneys' fees), and rescissory damages. In April 2002, plaintiffs filed a consolidated amended class action complaint against us and certain of our current and former board members and/or officers. The consolidated amended class action complaint includes similar allegations to those described above and seeks similar relief. In July 2002, we moved to dismiss the consolidated amended class action complaint. In October 2002, pursuant to a stipulation and tolling agreement with plaintiffs, our current and former board members and/or officers were dismissed without prejudice. In February 2003, the court denied our motion to dismiss the consolidated amended class action complaint. In June 2003, we approved a proposed Memorandum of Understanding among the plaintiffs, issuers and insurers as to terms for a settlement of the litigation against us which was further documented in a Stipulation and Agreement of Settlement filed with the court. The proposed settlement terms would not require Stamps.com to make any payments. The proposed settlement was preliminarily approved by the court in February 2005, was the subject of fairness hearing in April 2006, but remains subject to final approval by the court which has not yet occurred.

In addition to the class action lawsuits against us, over 1,000 similar lawsuits have also been brought against over 250 companies which issued stock to the public in 1998, 1999, and 2000, and their underwriters. These lawsuits (including those naming us) followed publicized reports that the Securities and Exchange Commission was investigating the practice of certain underwriters in connection with initial public offerings. All of these lawsuits have been consolidated for pretrial purposes before United States District Court Judge Shira Scheindlin of the Southern District of New York. We have placed our underwriters on notice of our rights to indemnification, pursuant to our agreements with the underwriters, but under the terms of the proposed settlement, we cannot assert these claims except as a defense to a claim against us by the underwriters. We have also provided notice to our directors' and officers' insurers who have agreed to fund the proposed settlement. If the proposed settlement does not receive final approval or is not consummated for any reason, we intend to defend the lawsuits vigorously because we believe that the claims against us and our officers and directors are without merit.

We are not currently involved in any other material legal proceedings, nor are we aware of any other material legal proceedings pending against us.

ITEM 1A. RISK FACTORS

You should carefully consider the following risks and the other information in this Report and our other filings with the SEC before you decide to invest in our company or to maintain or increase your investment. The risks and uncertainties described below are not the only ones facing Stamps.com. Additional risks and uncertainties may also adversely impact and impair our business. If any of the following risks actually occur, our business, results of operations or financial condition would likely suffer. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment.

This Report contains forward-looking statements based on the current expectations, assumptions, estimates and projections about Stamps.com and the Internet. These forward-looking statements involve risks and uncertainties. Our actual results could differ materially from those discussed in these forward-looking statements as a result of many factors, including those described in this section and elsewhere in this Report. Stamps.com does not undertake to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.

Risks Related to Our Business

We may not successfully implement strategies to increase the adoption of our services and products which would limit our growth, adversely affect our business and cause the price of our common stock to decline.

Our continuing profitability depends on our ability to successfully implement our strategy of increasing the adoption of our services and products. Factors that might cause our revenues, margins and operating results to fluctuate include the factors described in the subheadings below as well as:

- The costs of our marketing programs to establish and promote the Stamps.com brands;
- The demand for our services and products;
- Our ability to develop and maintain strategic distribution relationships;
- The number, timing and significance of new products or services introduced by us and by our competitors;
- Our ability to develop, market and introduce new and enhanced products and services on a timely basis;
- The level of service and price competition;
- Our operating expenses;
- US Postal Service regulation and policies relating to PC Postage and PhotoStamps; and
- General economic factors.

We have a history of losses and we may incur losses in the future which may reduce the trading price of our common stock.

Though we realized net income of $4.2 million and $2.1 million for the three months ended June 30, 2006 and 2005 respectively, we have experienced significant net losses since our inception and we may experience net losses in the future. Although we achieved profitability during fiscal year 2005, we cannot be certain that we will be able to sustain or increase such profitability in the future.

We implemented pricing plans that may adversely affect our future revenues and margins.

Our ability to generate gross margins depends upon the ability to generate significant revenues from a large base of active customers. In order to attract customers in the future, we may run special promotions and offers such as free trials, discounts on fees, postage and supplies, and other promotions. We cannot be sure that customers will be receptive to future fee structures and special promotions that we may implement. Even though we have established a sizeable base of users, we still may not generate sufficient gross margins to remain profitable. In addition, our ability to generate revenues or sustain profitability could be adversely affected by the special promotions or additional changes to our pricing plans.

If we do not successfully attract and retain skilled personnel for permanent management and other key personnel positions, we may not be able to effectively implement our business plan.

Our success depends largely on the skills, experience and performance of the members of our senior management and other key personnel. Any of the individuals can terminate his or her employment with us at any time. If we lose key employees and are unable to replace them with qualified individuals, our business and operating results could be seriously harmed. In addition, our future success will depend largely on our ability to continue attracting and retaining highly skilled personnel. As a result, we may be unable to successfully attract, assimilate or retain qualified personnel. Further, we may be unable to retain the employees we currently employ or attract additional qualified personnel to replace those key employees that may depart. The failure to attract and retain the necessary personnel could seriously harm our business, financial condition and results of operations.

The success of our business will depend upon the continued acceptance by customers of our service.

We must minimize the rate of loss of existing customers while adding new customers. Customers cancel their subscription to our service for many reasons, including a perception that they do not use the service sufficiently that the costs for service are too high, because they are going out of business, or other issues that are not satisfactorily resolved. We must continually add new customers both to replace customers who cancel and to continue to grow our business beyond our current customer base. If too many of our customers cancel our service, or if we are unable to attract new customers in numbers sufficient to grow our business, our operating results will be adversely affected. Further, if excessive numbers of customers cancel our service, we may be required to incur significantly higher marketing expenditures than we currently anticipate to replace these customers with new customers.

If we fail to effectively market and sell our services and products, our business will be substantially harmed and could fail.

In order to acquire customers and achieve widespread distribution and use of our services and products, we must develop and execute cost-effective marketing campaigns and sales programs. We currently rely on a combination of marketing techniques to attract new customers including direct mail, online marketing and business partnerships. We may be unable to continue marketing our services and products in a cost-effective manner. If we fail to acquire customers in a cost-effective manner, our results of operations will be adversely affected.

If we fail to meet the demands of our customers, our business will be substantially harmed and could fail.

Our services and products must meet the commercial demands of our customers, which include home businesses, small businesses, corporations and individuals. We cannot be sure that our services will appeal to or be adopted by an ever-growing range of customers. If we are unable to ship products such as items from our Supplies Store or PhotoStamps in a timely manner to our customers, our business may be harmed. Moreover, our ability to obtain and retain customers depends, in part, on our customer service capabilities. If we are unable at any time to address customer service issues adequately or to provide a satisfactory customer experience for current or potential customers, our business and reputation may be harmed. If we fail to meet the demands of our customers our results of operations will be adversely affected.

A failure to further develop and upgrade our services and products could adversely affect our business.

Any delays or failures in developing our services and products, including upgrades of current services and products, may have a harmful impact on our results of operations. The need to extend our core technologies into new features and services and to anticipate or respond to technological changes could affect our ability to develop these services and features. Delays in features or upgrade introductions could cause a decline in our revenue, earnings or stock price. We cannot determine the ultimate effect these delays or the introduction of new features or upgrades will have on our revenue or results of operations.

Third party assertions of violations of their intellectual property rights could adversely affect our business.

Substantial litigation regarding intellectual property rights exists in our industry. Third parties may currently have, or may eventually be issued, patents upon which our products or technology infringe. Any of these third parties might make a claim of infringement against us. We may become aware of, or we may increasingly receive correspondence claiming, potential infringement of other parties' intellectual property rights. We could incur significant costs and diversion of management time and resources to defend claims against us regardless of their validity. Any associated costs and distractions could have a material adverse effect on our business, financial condition and results of operations. In addition, litigation in which we are accused of infringement might cause product development delays, require us to develop non-infringing technology or require us to enter into royalty or license agreements, which might not be available on acceptable terms, or at all. If a successful claim of infringement were made against us and we could not develop non-infringing technology or license the infringed or similar technology on a timely and cost-effective basis, our business could be significantly harmed or fail. Any loss resulting from intellectual property litigation could severely limit our operations, cause us to pay license fees, or prevent us from doing business.

A failure to protect our own intellectual property could harm our competitive position.

We rely on a combination of patent, trade secret, copyright and trademark laws and contractual restrictions, such as confidentiality agreements and licenses, to establish and protect our rights in our products, services, know-how and information. We have 56 issued US patents, 77 pending US patent applications, 9 international patents and 20 pending international patent applications. We also have a number of registered and unregistered trademarks. We plan to apply for more patents in the future. We may not receive patents for any of our patent applications. Even if patents are issued to us, claims issued in these patents may not protect our technology. In addition, a court might hold any of our patents, trademarks or service marks invalid or unenforceable. Even if our patents are upheld or are not challenged, third parties may develop alternative technologies or products without infringing our patents. If our patents fail to protect our technology or our trademarks and service marks are successfully challenged, our competitive position could be harmed. We also generally enter into confidentiality agreements with our employees, consultants and other third parties to control and limit access and disclosure of our confidential information. These contractual arrangements or other steps taken to protect our intellectual property may not prove to be sufficient to prevent misappropriation of technology or deter independent third party development of similar technologies. Additionally, the laws of foreign countries may not protect our services or intellectual property rights to the same extent as do the laws of the United States.

System and online security failures could harm our business and operating results.

Our services depend on the efficient and uninterrupted operation of our computer and communications hardware systems. In addition, we must provide a high level of security for the transactions we execute. We rely on internally-developed and third-party technology to provide secure transmission of postage and other confidential information. Any breach of these security measures would severely impact our business and reputation and would likely result in the loss of customers. Furthermore, if we are unable to provide adequate security, the US Postal Service could prohibit us from selling postage over the Internet.

Our systems and operations are vulnerable to damage or interruption from a number of sources, including fire, flood, power loss, telecommunications failure, break-ins, earthquakes and similar events. Our Internet host provider does not guarantee that our Internet access will be uninterrupted, error-free or secure. Our servers are also vulnerable to computer viruses, physical, electrical or electronic break-ins and similar disruptions. We have experienced minor system interruptions in the past and may experience them again in the future. Any substantial interruptions in the future could result in the loss of data and could completely impair our ability to generate revenues from our service. We do not presently have a full disaster recovery plan in effect to cover the loss of facilities and equipment. In addition, we do not have a fail-over site that mirrors our infrastructure to allow us to operate from a second location.

We have business interruption insurance; however, we cannot be certain that our coverage will be sufficient to compensate us for losses that may occur as a result of business interruptions.

A significant barrier to electronic commerce and communications is the secure transmission of confidential information over public networks. Anyone who is able to circumvent our security measures could misappropriate confidential information or cause interruptions in our operations. We may be required to expend significant capital and other resources to protect against potential security breaches or to alleviate problems caused by any breach. We rely on specialized technology from within our own infrastructure to provide the security necessary for secure transmission of postage and other confidential information. Advances in computer capabilities, new discoveries in security technology, or other events or developments may result in a compromise or breach of the algorithms we use to protect customer transaction data. Should someone circumvent our security measures, our reputation, business, financial condition and results of operations could be seriously harmed. Security breaches could also expose us to a risk of loss or litigation and possible liability for failing to secure confidential customer information. As a result, we may be required to expend a significant amount of financial and other resources to protect against security breaches or to alleviate any problems that they may cause.

Risks Related to Our Industry

US Postal Service regulations or fee assessments may cause disruptions or discontinuance of our business.

We are subject to continued US Postal Service scrutiny and other government regulations. The availability of our services is dependent upon our service continuing to meet US Postal Service performance specifications and regulations. The US Postal Service could change its certification requirements or specifications for PC Postage or revoke or suspend the approval of one or more of our services at any time. If at any time our service fails to meet US Postal Service requirements, we may be prohibited from offering this service and our business would be severely and negatively impacted. In addition, the US Postal Service could suspend or terminate our approval or offer services which compete against us, any of which could stop or negatively impact the commercial adoption of our service. Any changes in requirements or specifications for PC Postage could adversely affect our pricing, cost of revenues, operating results and margins by increasing the cost of providing our service.

The US Postal Service could also decide that PC Postage should no longer be an approved postage service due to security concerns or other issues. Our business would suffer dramatically if we are unable to adapt our services to any new requirements or specifications or if the US Postal Service were to discontinue PC Postage as an approved postage method. Alternatively, the US Postal Service could introduce competitive programs or amend PC Postage requirements to make certification easier to obtain, which could lead to more competition from third parties or the US Postal Service itself. If we are unable to compete successfully, particularly against large, traditional providers of postage products like Pitney Bowes who enter the online postage market, our revenues and operating results will suffer.

The US Postal Service could decide to suspend or cancel the current market test of PhotoStamps, and may do so in the event that there is sufficient cause to believe that the market test presents unacceptable risk to US Postal Service revenues, degrades the ability of the US Postal Service to process or deliver mail produced by the test participants, exposes the US Postal Service or its customers to legal liability, or causes public or political embarrassment or harm to the US Postal Service in any way. If the US Postal Service decides to suspend or cancel the market test of PhotoStamps, our revenues and operating results will likely suffer.

Additionally, the US Postal Service could decide to amend, renegotiate or terminate our credit card cost sharing agreement, which is a key agreement that governs the allocation of credit card fees paid by the US Postal Service and us for the postage purchased by our customers. If the US Postal Service decides to amend, renegotiate or terminate our credit card cost sharing agreement, our revenues and operating results will likely suffer.

In addition, US Postal Service regulations may require that our personnel with access to postal information or resources receive security clearance prior to doing relevant work. We may experience delays or disruptions if our personnel cannot receive necessary security clearances in a timely manner, if at all. The regulations may limit our ability to hire qualified personnel. For example, sensitive clearance may only be provided to US citizens or aliens who are specifically approved to work on US Postal Service projects.

If we are unable to compete successfully, particularly against large, traditional providers of postage products such as Pitney Bowes, our revenues and operating results will suffer.

The PC Postage segment of the market for postage is relatively new and is competitive. At present, Pitney Bowes and Endicia.com are authorized PC Postage providers with commercially available software and Zazzle.com offers a competitive product to PhotoStamps using Pitney Bowes technology. If any more providers become authorized, or if Pitney Bowes or Endicia.com provide enhanced offerings, our operations could be adversely impacted. We also compete with other forms of postage, including traditional postage meters provided by companies such as Pitney Bowes, postage stamps and permit mail.

We may not be able to establish or maintain a competitive position against current or future competitors as they enter the market. Many of our competitors have longer operating histories, larger customer bases, greater brand recognition, greater financial, marketing, service, support, technical, intellectual property and other resources than us. As a result, our competitors may be able to devote greater resources to marketing and promotional campaigns, adopt more aggressive pricing policies and devote substantially more resources to web site and systems development than us. This increased competition may result in reduced operating margins, loss of market share and a diminished brand. We may from time to time make pricing, service or marketing decisions or acquisitions as a strategic response to changes in the competitive environment. These actions could result in reduced margins and seriously harm our business.

We could face competitive pressures from new technologies or the expansion of existing technologies approved for use by the US Postal Service. We may also face competition from a number of indirect competitors that specialize in electronic commerce and other companies with substantial customer bases in the computer and other technical fields. Additionally, companies that control access to transactions through a network or Web browsers could also promote our competitors or charge us a substantial fee for inclusion. In addition, changes in postal regulations could adversely affect our service and significantly impact our competitive position. We may be unable to compete successfully against current and future competitors, and the competitive pressures we face could seriously harm our business.

If we do not respond effectively to technological change, our services and products could become obsolete and our business will suffer.

The development of our services, products and other technology entails significant technical and business risks. To remain competitive, we must continue to enhance and improve the responsiveness, functionality and features of our online operations. The Internet and the electronic commerce industry are characterized by rapid technological change; changes in user and customer requirements and preferences; frequent new product and service introductions embodying new technologies; and the emergence of new industry standards and practices.

The evolving nature of the Internet or the postage markets could render our existing technology and systems obsolete. Our success will depend, in part, on our ability to license or acquire leading technologies useful in our business; enhance our existing services; develop new services or features and technology that address the increasingly sophisticated and varied needs of our current and prospective users; and respond to technological advances and emerging industry and regulatory standards and practices in a cost-effective and timely manner.

Future advances in technology may not be beneficial to, or compatible with, our business. Furthermore, we may not be successful in using new technologies effectively or adapting our technology and systems to user requirements or emerging industry standards on a timely basis. Our ability to remain technologically competitive may require substantial expenditures and lead time. If we are unable to adapt in a timely manner to changing market conditions or user requirements, our business, financial condition and results of operations could be seriously harmed.

Our operating results could be impaired if we or the Internet become subject to additional government regulation and legal uncertainties.

Due to the increasing popularity and use of the Internet, it is possible that a number of laws and regulations may be adopted with respect to the Internet, relating to user privacy, pricing, content, copyrights, distribution, characteristics and quality of products and services, and export controls.

The adoption of any additional laws or regulations may hinder the expansion of the Internet. A decline in the growth of the Internet could decrease demand for our products and services and increase our cost of doing business. Moreover, the applicability of existing laws to the Internet is uncertain with regard to many issues, including property ownership, export of specialized technology, sales tax, libel and personal privacy. Our business, financial condition and results of operations could be seriously harmed by any new legislation or regulation. The application of laws and regulations from jurisdictions whose laws do not currently apply to our business, or the application of existing laws and regulations to the Internet and other online services could also harm our business.

We have employees and offer our services in multiple states, and we may in the future expand internationally. These jurisdictions may claim that we are required to qualify to do business as a foreign corporation in each state or foreign country. Our failure to qualify as a foreign corporation in a jurisdiction where we are required to do so could subject us to taxes and penalties. Other states and foreign countries may also attempt to regulate our services or prosecute us for violations of their laws. Further, we might unintentionally violate the laws of foreign jurisdictions and those laws may be modified and new laws may be enacted in the future.

Risks Related to Our Stock

Changes in stock option accounting rules will have an adverse affect on our operating results.

We use options to acquire our common stock to attract, incentivize and retain our employees in a competitive marketplace. Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation," allowed companies the choice of either using a fair value method of accounting for options that would result in expense recognition for all options granted, or using an intrinsic value method, as prescribed by Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees", with a pro forma disclosure of the impact on net income (loss) of using the fair value option expense recognition method. Prior to our adoption of SFAS No. 123 (revised 2004), "Share Based Payment," or Statement 123R, on January 1, 2006, we had elected to apply APB No.25 and accordingly we generally did not recognize any expense with respect to employee options to acquire our common stock in periods ended on or prior to December 31, 2005 as long as such options were granted at exercise prices equal to the fair value of our common stock on the date of grant.

In December 2004, the Financial Accounting Standards Board ("FASB") issued Statement 123R. Statement 123R requires that the compensation cost relating to share-based payment transactions be recognized in financial statements. This cost will be measured based on the fair value of the equity instruments issued. We adopted Statement 123R on January 1, 2006, which is the first day of our 2006 fiscal year. We expect the adoption of Statement 123R to have an adverse effect on our operating results, as we continue to use options to attract, incentivize and retain our employees.

The tax value of our net operating losses could be impaired if we trigger a change of control pursuant to Section 382 of the Internal Revenue Code.

Under the complicated rules of IRC Section 382, a change in ownership can occur whenever there is a shift in ownership by more than 50% by one or more five-percent shareholders within a three-year period. If a change of ownership is triggered, our NOLs may be impaired, which could harm stockholder value.

Our charter documents could deter a takeover effort, which could inhibit your ability to receive an acquisition premium for your shares.

The provisions of our certificate of incorporation, bylaws and Delaware law could make it difficult for a third party to acquire us, even if it would be beneficial to our stockholders. In addition, we are subject to the provisions of Section 203 of the Delaware General Corporation Law, which could prohibit or delay a merger or other takeover of our Company, and discourage attempts to acquire us.

The US Postal Service may object to a change of control of our common stock.

The US Postal Service may raise national security or similar concerns to prevent foreign persons from acquiring significant ownership of our common stock or of Stamps.com. The US Postal Service also has regulations regarding the change of control of approved PC Postage providers. These concerns may prohibit or delay a merger or other takeover of our Company. Our competitors may also seek to have the US Postal Service block the acquisition by a foreign person of our common stock or our Company in order to prevent the combined company from becoming a more effective competitor in the market for PC Postage.

Our stock price is volatile

The price at which our common stock has traded since our initial public offering in June 1999 has fluctuated significantly. The price may continue to be volatile due to a number of factors, including the following, some of which are beyond our control:

- variations in our operating results,
- variations between our actual operating results and the expectations of securities analysts,
- investors and the financial community,
- announcements of developments affecting our business, systems or expansion plans by us or others,

· and market volatility in general.

As a result of these and other factors, investors in our common stock may not be able to resell their shares at or above their original purchase price. In the past, securities class action litigation often has been instituted against companies following periods of volatility in the market price of their securities. This type of litigation, if directed at us, could result in substantial costs and a diversion of management's attention and resources.

Shares of our common stock held by existing stockholders may be sold into the public market, which could cause the price of our common stock to decline.

If our stockholders sell into the public market substantial amounts of our common stock purchased in private financings prior to our initial public offering, or purchased upon the exercise of stock options or warrants, or if there is a perception that these sales could occur, the market price of our common stock could decline. All of these shares are available for immediate sale, subject to the volume and other restrictions under Rule 144 of the Securities Act of 1933.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The annual meeting of Stamps.com's stockholders was held on June 7, 2006. At that meeting, two proposals were submitted to a vote of the stockholders: (1) to elect two directors (G. Bradford Jones and Lloyd I. Miller) to serve for a three-year term ending in the year 2009 or until their successors are duly elected and qualified; and (2) to ratify the appointment of Ernst & Young LLP as our independent auditors for the fiscal year ending December 31, 2006.

At the close of business on the record date for the meeting (which was April 14, 2006), there were 23,869,172 shares of common stock outstanding and entitled to be voted at the meeting. Holders of 22,392,852 shares of common stock (representing a like number of votes) were present at the meeting, either in person or by proxy. The following table sets forth the results of the voting:

Proposal	For	Withheld
Election of two directors:		
G. Bradford Jones	21,889,656	503,196
Lloyd I. Miller	21,889,606	503,246

Proposal	For	Against	Abstain
Appointment of Ernst & Young LLP(auditors)	22,344,468	42,899	5,485

Each of the proposals set forth above received more than the required number of votes for approval and were therefore duly and validly approved by the stockholders.

ITEM 5. OTHER INFORMATION

On July 26, 2006, Stamps.com filed a report on Form 8-K, which reported earnings for the quarter ended June 30, 2006.

ITEM 6. EXHIBITS

31.1 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

STAMPS.COM INC.
(Registrant)

August 9, 2006	By: /s/ KEN MCBRIDE **Ken McBride** **Chief Executive Officer**
August 9, 2006	By: /s/ KYLE HUEBNER **Kyle Huebner** **Chief Financial Officer**