MODEL N, INC.
Form 10-Q
August 09, 2013
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2013

OR

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

For the transition period from _________ to _________

Commission File Number: 001-35840

Model N, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**77-0528806**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
1800 Bridge Parkway Redwood City, California	**94065**
(Address of Principal Executive Offices)	**(Zip Code)**

(650) 610-4600

(Registrant s Telephone Number, Including Area Code)

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 x No ¨

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

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

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

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

As of July 31, 2013, the registrant had 22,953,700 shares of common stock issued and outstanding.

Table of Contents

TABLE OF CONTENTS

		Page
PART I. FINANCIAL INFORMATION		
Item 1.	Financial Statements (Unaudited)	1
	Condensed Consolidated Balance Sheets as of June 30, 2013 and September 30, 2012	1
	Condensed Consolidated Statements of Operations for the Three and Nine Months Ended June 30, 2013 and 2012	2
	Condensed Consolidated Statements of Comprehensive Income (Loss) for the Three and Nine Months Ended June 30, 2013 and 2012	3
	Condensed Consolidated Statements of Cash Flows for the Nine Months Ended June 30, 2013 and 2012	4
	Notes to Condensed Consolidated Financial Statements	5
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	14
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	24
Item 4.	Controls and Procedures	25
PART II. OTHER INFORMATION		
Item 1.	Legal Proceedings	26
Item 1A.	Risk Factors	26
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	43
Item 3.	Defaults Upon Senior Securities	43
Item 4.	Mine Safety Disclosures	43
Item 5.	Other Information	43
Item 6.	Exhibits	43
	Signatures	44

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

MODEL N, INC.

Condensed Consolidated Balance Sheets

(in thousands, except per share data)

(Unaudited)

	As of June 30, 2013	As of September 30, 2012
Assets		
Current Assets:		
Cash and cash equivalents	$ 105,078	$ 15,768
Short-term investments	59	
Accounts receivable, net	20,146	12,468
Deferred cost of implementation services, current portion	1,121	1,077
Prepaid expenses	2,124	2,246
Other current assets	138	552
Total current assets	128,666	32,111
Property and equipment, net	6,913	4,590
Goodwill	1,509	1,509
Intangible assets, net	1,001	1,248
Other assets	686	1,140
Total assets	$ 138,775	$ 40,598
Liabilities, Convertible Preferred Stock And Stockholders Equity (Deficit)		
Current Liabilities:		
Accounts payable	$ 2,282	$ 196
Accrued employee compensation	10,419	7,650
Accrued liabilities	3,523	4,432
Deferred revenue, current portion	25,854	29,362
Capital lease obligations, current portion	433	555
Loan obligations, current portion		2,500
Total current liabilities	42,511	44,695
Deferred revenue, net of current portion	4,341	2,289
Capital lease obligations, net of current portion	29	349
Loan obligations, net of current portion		2,627
Other long-term liabilities	684	1,125
Total liabilities	47,565	51,085
Commitments and contingencies		
Convertible Preferred Stock:		
Convertible preferred stock, $0.00005 par value; no shares and 20,571 shares authorized, no shares and 20,103 shares issued and outstanding as of June 30, 2013 and September 30, 2012, respectively		41,776
Stockholders Equity (Deficit):		
Common Stock, $0.00015 par value; 200,000 and 100,000 shares authorized as of June 30, 2013 and September 30, 2012, respectively; 22,946 and 8,131 shares issued and outstanding as of June 30, 2013 and September 30, 2012, respectively	3	1
Preferred Stock, $0.00015 par value; 5,000 shares authorized, no shares issued and outstanding		
Additional paid-in capital	154,312	9,045
Accumulated other comprehensive loss	(242)	(120)

Accumulated deficit	(62,863)	(61,189)
Total stockholders equity (deficit)	91,210	(52,263)
Total liabilities, convertible preferred stock and stockholders equity (deficit)	$ 138,775	$ 40,598

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

1

Table of Contents

MODEL N, INC.

Condensed Consolidated Statements of Operations

(in thousands, except per share data)

(Unaudited)

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Nine Months Ended June 30, 2013	Nine Months Ended June 30, 2012
Revenues:				
License and implementation	$ 16,419	$ 13,191	$ 43,362	$ 36,215
SaaS and maintenance	10,828	9,582	30,785	24,855
Total revenues	27,247	22,773	74,147	61,070
Cost of Revenues:				
License and implementation	7,527	5,712	19,887	16,255
SaaS and maintenance	4,865	5,616	14,169	13,280
Total cost of revenues	12,392	11,328	34,056	29,535
Gross profit	14,855	11,445	40,091	31,535
Operating Expenses:				
Research and development	4,063	4,491	12,665	13,481
Sales and marketing	5,256	5,356	16,362	15,042
General and administrative	3,883	2,618	11,518	7,784
Total operating expenses	13,202	12,465	40,545	36,307
Income (loss) from operations	1,653	(1,020)	(454)	(4,772)
Interest expense, net	85	160	326	514
Other (income) expenses, net	(48)	(36)	664	549
Income (loss) before income taxes	1,616	(1,144)	(1,444)	(5,835)
Provision for income taxes	81	92	230	231
Net income (loss)	$ 1,535	$ (1,236)	$ (1,674)	$ (6,066)
Net income (loss) per share attributable to common stockholders:				
Basic	$ 0.07	$ (0.16)	$ (0.12)	$ (0.78)
Diluted	$ 0.06	$ (0.16)	$ (0.12)	$ (0.78)
Weighted average number of shares used in computing net income (loss) per share attributable to common stockholders:				
Basic	22,798	7,912	13,647	7,754
Diluted	26,072	7,912	13,647	7,754

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

2

Table of Contents

MODEL N, INC.

Condensed Consolidated Statements of Comprehensive Income (Loss)

(in thousands)

(Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2013	2012	2013	2012
Net income (loss)	$ 1,535	$ (1,236)	$ (1,674)	$ (6,066)
Foreign currency translation loss, net of taxes	(98)	(86)	(122)	(61)
Total comprehensive income (loss)	$ 1,437	$ (1,322)	$ (1,796)	$ (6,127)

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

Table of Contents

MODEL N, INC.

Condensed Consolidated Statements of Cash Flows

(in thousands)

(Unaudited)

	Nine Months Ended June 30, 2013	Nine Months Ended June 30, 2012
Cash Flows From Operating Activities:		
Net loss	$ (1,674)	$ (6,066)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities		
Depreciation and amortization	1,414	1,083
Amortization of intangible assets	247	151
Stock-based compensation	3,306	2,005
Loss on disposal of property and equipment	2	
Amortization of debt discount	81	31
Changes in fair value of preferred stock warrant liability	671	355
Provision for doubtful accounts	9	(3)
Deferred income taxes	90	100
Changes in assets and liabilities		
Accounts receivable	(7,767)	306
Prepaid expenses and other current assets	(1,861)	(250)
Deferred cost of implementation services	305	(275)
Accounts payable	1,899	388
Accrued employee compensation	2,699	5,736
Other accrued and long-term liabilities	1,271	55
Deferred revenue	(1,376)	3,756
Net cash (used in) provided by operating activities	(684)	7,372
Cash Flows From Investing Activities		
Purchases of property and equipment	(811)	(1,026)
Capitalization of software development costs	(2,698)	(520)
Purchase of short-term investments	(63)	
Acquisition of a business		(3,000)
Net cash used in investing activities	(3,572)	(4,546)
Cash Flows From Financing Activities		
Proceeds from initial public offering, net of underwriting discounts and commissions of $7.6 million	101,064	
Proceeds from issuance of common stock upon exercise of stock options	768	587
Payments for deferred offering costs	(2,562)	
Principal payments on capital lease obligations	(442)	(419)
Principal payments on loan	(5,208)	(1,667)
Net cash provided by (used in) financing activities	93,620	(1,499)
Effect of exchange rate changes on cash and cash equivalents	(54)	(44)
Net increase in cash and cash equivalents	89,310	1,283
Cash and cash equivalents		
Beginning of the period	15,768	18,420
End of the period	$ 105,078	$ 19,703
Noncash Investing and Financing Activities:		
Acquisition of property and equipment under capital leases	$	$ 95
Capitalized stock options in software development costs	104	5
Issuance of convertible preferred stock warrant in connection with loan financing		160
Net settlement for exercise of common stock warrant	300	
Deferred offering costs not yet paid	385	

Conversion of convertible preferred stock to common stock	41,776
Conversion of preferred stock warrant to common stock warrant	1,419

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

Table of Contents

MODEL N, INC.

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. The Company and Significant Accounting Policies and Estimates

Model N, Inc. (Company) was incorporated in Delaware on December 14, 1999. The Company is a provider of revenue management solutions for the life science and technology industries. The Company s solutions enable its customers to maximize revenues and reduce revenue compliance risk by transforming their revenue life cycle from a series of tactical, disjointed operations into a strategic end-to-end process, which enables them to manage the strategy and execution of pricing, contracting, incentives and rebates. The Company s corporate headquarters are located in Redwood City, California, with additional offices in the United States, India, the United Kingdom and Switzerland.

Fiscal Year

The Company s fiscal year ends on September 30. References to fiscal year 2013, for example, refer to the fiscal year ending September 30, 2013.

Initial Public Offering

On March 25, 2013, the Company closed its initial public offering (IPO) whereby 7,751,000 shares of common stock were sold to the public (inclusive of 1,011,000 shares of common stock pursuant to the full exercise of an overallotment option granted to the underwriters and 740,000 shares of common stock sold by a selling stockholder). The aggregate net proceeds received by the Company from the offering were $101.1 million, net of underwriting discounts and commissions. Upon the closing of the IPO, all shares of the Company s outstanding convertible preferred stock automatically converted into 7,249,987 shares of common stock, and an outstanding warrant to purchase convertible preferred stock automatically converted into a warrant to purchase 86,655 shares of common stock. In May 2013, the warrant was converted into 71,847 shares of common stock, net of the warrant price.

Basis for Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (U.S. GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting. Certain information and note disclosures normally included in the financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. The condensed consolidated balance sheet data as of September 30, 2012 was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the prospectus filed with the SEC on March 20, 2013 pursuant to Rule 424(b) under the Securities Act of 1933 (Prospectus). There have been no changes in the significant accounting policies from those that were disclosed in the audited consolidated financial statements for the fiscal year ended September 30, 2012 included in the Prospectus filed with the SEC.

In the opinion of management, all normal recurring adjustments necessary to present fairly the condensed consolidated balance sheet as of June 30, 2013; the condensed consolidated statements of operations for the three and nine months ended June 30, 2013 and 2012; the condensed consolidated statements of comprehensive income (loss) for the three and nine months ended June 30, 2013 and 2012; and the condensed consolidated statements of cash flows for the nine months ended June 30, 2013 and 2012; have been made. The results of operations for the three and nine months ended June 30, 2013 are not necessarily indicative of the operating results for the full fiscal year 2013 or any future periods.

The Company s condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany transactions and balances have been eliminated upon consolidation.

Table of Contents

Use of Estimates

The preparation of the accompanying condensed consolidated financial statements in conformity with U.S. GAAP requires management to make certain estimates and assumptions that affect the amounts of assets and liabilities reported, disclosures about contingent assets and liabilities, and reported amounts of revenues and expenses during the reporting periods. Significant items subject to such estimates include revenue recognition, legal contingencies, income taxes, stock-based compensation, software development costs, valuation of intangibles, valuation of common stock and valuation of the convertible preferred stock warrant. These estimates and assumptions are based on management s best estimates and judgment. Management regularly evaluates its estimates and assumptions using historical experience and other factors; however, actual results could differ significantly from these estimates.

Revenue Recognition

Revenues are comprised of license and implementation revenues and Software as a Service (SaaS) and maintenance revenues.

License and Implementation

License and implementation revenues include revenues from the sale of perpetual software licenses for the Company s solutions and related implementation services. Based on the nature and scope of the implementation services, the Company has concluded that generally the implementation services are essential to its customers usability of its on-premise solutions, and therefore, the Company recognizes revenues from the sale of software licenses for its on-premise solutions and related implementation services on a percentage-of-completion basis over the expected implementation period. The Company estimates the length of this period based on a number of factors, including the number of licensed applications and the scope and complexity of the customer s deployment requirements. The percentage-of-completion computation is measured by the hours expended on the implementation of the Company s software solutions during the reporting period as a percentage of the total hours estimated to be necessary to complete the implementation of the Company s software solutions.

SaaS and Maintenance

SaaS and maintenance revenues primarily include subscription and related implementation fees from customers accessing the Company s cloud-based solutions and revenues associated with maintenance and support contracts from customers using on-premise solutions. Also included in SaaS and maintenance revenues are other revenues, including revenues related to application support, training and customer-reimbursed expenses.

SaaS arrangements include multiple elements, comprised of subscription fees and related implementation services. In SaaS arrangements where implementation services are complex and do not have a stand-alone value to the customers, the Company considers the entire arrangement consideration, including subscription fees and related implementation services, as a single unit of accounting in accordance with the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2009-13, Revenue Recognition (Accounting Standards Codification (ASC) Topic 605) Multiple-Deliverable Revenue Arrangements. In such arrangements, the Company recognizes SaaS revenues ratably beginning the day the customer is provided access to the subscription service through the longer of the initial contractual period or term of the expected customer relationship.

In SaaS arrangements where subscription fees and implementation services have a standalone value, the Company allocates revenue to each element in the arrangement based on a selling price hierarchy. The selling price for a deliverable is based on its vendor-specific objective evidence (VSOE), if available, third-party evidence (TPE), if VSOE is not available, or best estimated selling price (BESP), if neither VSOE nor TPE is available. As the Company has been unable to establish VSOE or TPE for the elements of its arrangements, the Company establishes the BESP for each element by considering company-specific factors such as existing pricing and discounting. The consideration allocated to subscription fees is recognized as revenue ratably over the contract period. The consideration allocated to implementation services is recognized as revenue as services are performed. The total arrangement fee for a multiple element arrangement is allocated based on the relative BESP of each element.

Table of Contents

Maintenance and support revenues include post-contract customer support and the right to unspecified software updates and enhancements on a when and if available basis. Application support revenues include post-contract customer support for our software solutions, including support for any customer-specific configurations. Maintenance and support revenues, and application support revenues are recognized ratably over the period in which the services are provided. The revenues from training and customer-reimbursed expenses are recognized as the Company delivers these services.

Revenue Recognition

The Company commences revenue recognition when all of the following conditions are satisfied: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed or determinable and collection is probable. However, determining whether and when some of these criteria have been satisfied often involves assumptions and judgments that can have a significant impact on the timing and amount of revenues the Company reports.

For multiple software element arrangements, the Company allocates the sales price among each of the deliverables using the residual method, under which revenue is allocated to undelivered elements based on their vendor-specific objective evidence (VSOE) of fair value. VSOE is the price charged when an element is sold separately or a price set by management with the relevant authority. The Company has established VSOE for maintenance and support, application support and training.

The Company does not offer any contractual rights of return, rebates or price protection. The Company s implementation projects generally have a term ranging from a few months to three years and may be terminated by the customer at any time. Should a loss be anticipated on a contract, the full amount of the loss is recorded when the loss is determinable. The Company updates its estimates regarding the completion of implementations based on changes to the expected contract value and revisions to its estimates of time required to complete each implementation project. Amounts that may be payable to customers to settle customer disputes are recorded as a reduction in revenues or reclassified from deferred revenue to customer payables in other accrued liabilities.

Recent Accounting Pronouncements

There have been no developments to recently issued accounting standards, including the expected dates of adoption and estimated effects on the Company s consolidated financial statements, from those disclosed in the Prospectus, except for the following:

In March 2013, the FASB issued ASU No. 2013-05 *Parent s Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity* to resolve the diversity in practice regarding the release into net income of the cumulative translation adjustment upon derecognition of a subsidiary or group of assets within a foreign entity. This update will be effective for fiscal years beginning after December 15, 2013. The Company does not expect the adoption of this update will have a material impact on its consolidated financial statements, absent any material transactions involving the derecognition of subsidiaries or groups of assets within a foreign entity.

In February 2013, the FASB issued ASU No. 2013-02 *Comprehensive Income: Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* to improve the reporting of reclassifications out of accumulated other comprehensive income. This update requires the effect of significant reclassifications out of accumulated other comprehensive income be shown by component only if the amount reclassified is required to be reclassified to net income under U.S. GAAP. If the reclassification to net income is not required under U.S. GAAP, an entity is required to cross-reference to other disclosures that provide additional details about those amounts. This update will be effective for fiscal years beginning after December 15, 2012. The Company does not expect the adoption of this update will have a material impact on its consolidated financial statements.

In October 2012, the FASB issued ASU No. 2012-04 *Technical Corrections and Improvements*. The amendments in this ASU cover a wide range of topics in the ASC. These amendments include technical corrections and improvements to the ASC and conforming amendments related to fair value measurements. The amendments in this update will be effective for fiscal years beginning after December 15, 2012. The Company does not expect this to have a material impact on its consolidated financial statements.

Table of Contents

2. Fair Value of Financial Instruments

The financial instruments of the Company consist primarily of cash and cash equivalents, short-term investments, accounts receivable, accounts payable and certain accrued liabilities. The Company regularly reviews its financial instruments portfolio to identify and evaluate such instruments that have indications of possible impairment. When there is no readily available market data, fair value estimates are made by the Company, which involves some level of management estimation and judgment and may not necessarily represent the amounts that could be realized in a current or future sale of these assets.

Based on borrowing rates currently available to the Company for financing obligations with similar terms and considering the Company s credit risks, the carrying value of the financing obligation approximates fair value.

Fair value is defined as the exchange price that would be received for an asset or an exit price paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The current accounting guidance for fair value instruments defines a three-level valuation hierarchy for disclosures as follows:

Level 1 Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 Input other than quoted prices included in Level 1 that are observable, unadjusted quoted prices in markets that are not active, or other inputs for similar assets and liabilities that are observable or can be corroborated by observable market data; and

Level 3 Unobservable inputs that are supported by little or no market activity, which require the Company to develop its own models and involves some level of management estimation and judgment.

The Company s Level 1 assets consist of United States treasury bills and certificates of deposit. These instruments are classified within Level 1 of the fair value hierarchy because they are valued based on quoted market prices in active markets.

The Company s Level 3 liabilities consist of a convertible preferred stock warrant (prior to the closing of the IPO on March 25, 2013) and contingent consideration payable in connection with a business acquisition. Contingent consideration payable in connection with a business acquisition is valued using a probability weighted expected payout model to determine the expected payout to calculate the fair value. The key assumptions in applying the approach are the internal forecasted sales and contributions for the acquired business, the probability of achieving the milestone and an appropriate discount rate.

The table below sets forth the Company s cash equivalents, short-term investments and liabilities as of June 30, 2013 and September 30, 2012, which are measured at fair value on a recurring basis by level within the fair value hierarchy. The assets are classified based on the lowest level of input that is significant to the fair value measurement.

	Level 1	Level 2	Level 3	Total
		(in thousands)		
As of June 30, 2013:				
Assets:				
Cash equivalents:				
Treasury bills	$ 95,504	$	$	$ 95,504
Short-term investments:				
Certificates of deposit	$ 59	$	$	$ 59
As of September 30, 2012:				
Assets:				
Cash equivalents:				
Money market funds	$ 14,387	$	$	$ 14,387
Liabilities:				
Contingent consideration in connection with a business acquisition	$	$	$ 354	$ 354
Convertible preferred stock warrant	$	$	$ 748	$ 748

The Company performed the final re-measurement of the convertible preferred stock warrant at the closing date of its IPO on March 25, 2013, and reclassified the warrant from other long-term liabilities to additional paid-in capital.

The Company decreased the balance of contingent consideration payable in connection with a business acquisition to zero and accordingly recognized a credit of $0.3 million for the nine months ended June 30, 2013 because the probability of achieving the milestone was considered remote.

Cash equivalents in the above table exclude $9.6 million and $1.4 million held in cash by the Company in its bank accounts as of June 30, 2013 and September 30, 2012, respectively.

There were no transfers of assets and liabilities measured at fair value between Level 1 and Level 2, or between Level 2 and Level 3, during the nine months ended June 30, 2013.

The following tables show the Company s available-for-sale securities adjusted cost, gross unrealized gains, gross unrealized losses and fair value recorded as cash and cash equivalents as of June 30, 2013:

	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
		(in thousands)		
Cash equivalents:				
Treasury bills	$ 95,504	$	$	$ 95,504

Table of Contents

3. Convertible Preferred Stock

Upon the closing of the IPO, all outstanding shares of convertible preferred stock were converted into shares of common stock, and an outstanding warrant to purchase convertible preferred stock automatically converted into a warrant to purchase 86,655 shares of common stock. In May 2013, the warrant was converted into 71,847 shares of common stock, net of the warrant price.

Convertible Preferred Stock Warrant

On October 19, 2010, in connection with a loan agreement, the Company issued a warrant to purchase 86,655 shares of the Company s Series C Preferred Stock at an exercise price of $3.462 per share. The warrant is exercisable in whole or in part at any time on or before the expiration date of the 10-year anniversary from the issuance date. Upon the closing of the IPO, this warrant automatically converted into a warrant to purchase the same number of shares of common stock at the same exercise price per share.

Prior to the closing of the IPO, the Company re-measured the fair value of the preferred stock warrant at each balance sheet date. The fair value of the outstanding warrant was classified within non-current liabilities on the condensed consolidated balance sheets, and any changes in fair value were recognized as a component of other (income) expenses, net in the consolidated statements of operations.

Upon the closing of the IPO, the warrant was reclassified from liability to equity and the Company will no longer record any mark-to-market changes in the fair value of the warrant. The Company performed the final re-measurement of the warrant on March 25, 2013, the closing date of the IPO, and recorded an expense of $0.7 million arising from the revaluation during the three months ended March 31, 2013. In May 2013, the warrant was converted into 71,847 shares of common stock, net of the warrant price.

The fair value of the outstanding warrant was determined using the Black-Scholes-Merton option-pricing model. The fair value of the warrant was estimated using the following assumptions for the periods presented below.

	Three Months Ended June 30,		**Nine Months Ended June 30,**	
	2013	**2012**	**2013**	**2012**
Risk-free interest rate		1.12%	0.92%	1.09%
Dividend yield				
Volatility		54%	45%	50%
Expected term (in years)		8.30	5.92	8.55

The change in the fair value of the convertible preferred stock warrant liability during the periods presented is summarized below.

	Three Months Ended June 30,		**Nine Months Ended June 30,**	
	2013	**2012**	**2013**	**2012**
	(in thousands)			
Opening balance	$	$ 846	$ 748	$ 403
Increase (decrease) in fair value		(88)	671	355
Reclassification of warrant to additional paid-in capital			(1,419)	
Closing balance	$	$ 758	$	$ 758

Table of Contents

4. Stock-based Compensation

The Company s board of directors (Board) adopted the 2013 Equity Incentive Plan (2013 Plan) in February 2013, and the stockholders approved the 2013 Plan in March 2013. The 2013 Plan became effective on March 18, 2013 and will terminate in February 2023. The 2013 Plan serves as the successor equity compensation plan to the 2010 Equity Incentive Plan (2010 Plan). The 2013 Plan was approved with a reserve of 8.0 million shares, which consists of 2.5 million shares of the Company s common stock reserved for future issuance under the 2013 Plan and shares of common stock previously reserved but unissued under the 2010 Plan. In addition, any shares of common stock subject to outstanding awards under the 2010 Plan and 2000 Plan that are issuable upon the exercise of options that expire without having been exercised in full, are forfeited or repurchased by us at the original purchase price or are used to pay the exercise price or withholding obligations related to any award will be available for future grant and issuance under the 2013 Plan. Additionally, the 2013 Plan provides for automatic increases in the number of shares available for issuance under it on October 1 of each of the first four calendar years during the term of the 2013 Plan by the lesser of 5% of the number of shares of common stock issued and outstanding on each September 30 immediately prior to the date of increase or the number determined by our board of directors. No further grants will be made under the 2010 Plan, and the balances under the 2010 Plan have been transferred to the 2013 Plan. The 2013 Plan provides for the grant of incentive stock options, nonqualified stock options, restricted stock awards, stock appreciation rights, performance stock awards, Restricted Stock Units and stock bonuses.

Stock-based compensation expenses were as follows:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2013	2012	2013	2012
Cost of services:				
License and implementation	$ 240	$ 61	$ 370	$ 207
SaaS and maintenance	215	77	403	469
Research and development	305	56	457	226
Sales and marketing	686	167	1,399	941
General and administrative	361	50	677	162
Total stock-based compensation expenses	$ 1,807	$ 411	$ 3,306	$ 2,005

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2013	2012	2013	2012
Stock options	$ 463	$ 235	$ 1,365	$ 951
Restricted stock awards (RSA)	175	181	528	1,059
Restricted stock units (RSU)	756		979	
Employee Stock Purchase Plan (ESPP)	476		538	
Total stock-based compensation	1,870	416	3,410	2,010
Less: Capitalized stock options	(63)	(5)	(104)	(5)
Total stock-based compensation expenses	$ 1,807	$ 411	$ 3,306	$ 2,005

The following table summarizes the stock option, RSU and restricted stock awards activities during the nine months ended June 30, 2013:

		Outstanding Awards			
	Shares Available for Grant	Number of Options	Weighted Average Exercise Price	Number of Restricted Stock Units	Number of Restricted Stock Awards
		(in thousands, except exercise price)			
Balance at September 30, 2012	982	4,559	$ 4.34	20	
Increase in shares reserved	2,761				
Granted	(1,299)	256	13.86	1,043	
Exercised/released		(484)	1.59		
Forfeited	224	(194)	8.72	(28)	(2)
Canceled					2

Expired	39	(39)	3.68	
Balance at June 30, 2013	2,707	4,098	$ 5.05	1,035

10

Table of Contents

Employee Stock Purchase Plan

The 2013 Employee Stock Purchase Plan (ESPP) became effective on March 19, 2013. The ESPP allows eligible employees to purchase shares of the Company s common stock at a discount through payroll deductions of up to 15% of their eligible compensation, at not less than 85% of the fair market value, as defined in the ESPP, subject to any plan limitations. Except for the initial offering period, the ESPP provides for six-month offering periods, starting on February 20 and August 20 of each year. The initial offering period began on March 19, 2013 and will end on February 19, 2014.

Restricted Stock Awards Issued to Certain Employees in Connection with the LeapFrogRx Acquisition

In January 2012, the Company issued 200,000 shares of common stock to certain employees of LeapFrogRx, Inc. (LeapFrogRx) in connection with the acquisition of LeapFrogRx. Of these shares, 64,445 and 133,333 shares were subject to repurchase as of June 30, 2013 and September 30, 2012, respectively.

Valuation Assumptions

The following table presents the weighted-average assumptions used to estimate the fair value of options granted during the period presented:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2013	**2012**	**2013**	**2012**
Risk-free interest rate	1.10%	1.12%	1.05%	1.08%
Dividend yield				
Volatility	49%	54%	49%	47%
Expected term (in years)	6.08	6.08	6.08	5.96

The expected terms of options granted were calculated using the simplified method, determined as the average of the contractual term and the vesting period. Estimated volatility is derived from the historical closing prices of common shares of similar entities whose share prices are publicly available for the expected term of the option. The risk-free interest rate is based on the U.S. Treasury constant maturities in effect at the time of grant for the expected term of the option. We use historical data to estimate the number of future stock option forfeitures.

The following table presents the weighted-average assumptions used to estimate the fair value of the ESPP during the period from March 19, 2013 to June 30, 2013:

Risk-free interest rate	0.15%
Dividend yield	
Volatility	36%
Expected term (in years)	0.92

5. Income Taxes

The Company recorded an income tax provision of $81,000, $92,000, $230,000 and $231,000 for the three months ended June 30, 2013 and 2012 and the nine months ended June 30, 2013 and 2012, respectively, representing effective income tax rates of 5%, (8)%, (16)% and (4)%, respectively. The Company s effective income tax rate during these periods differs from the Company s federal statutory rate of 34% primarily due to permanent differences for stock-based compensation and the impact of state income taxes and foreign tax rate differences.

Table of Contents

6. Net Income (Loss) per Share

The following table sets forth the computation of the Company s basic and diluted net income (loss) per share attributable to common stockholders under the two-class method during the period presented:

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Nine Months Ended June 30, 2013	Nine Months Ended June 30, 2012
	(in thousands, except share and per share data)			
Numerator:				
Net income (loss) attributable to common stockholders - Basic and diluted	$ 1,535	$ (1,236)	$ (1,674)	$ (6,066)
Denominator:				
Weighted average shares used in computing net income (loss) per share attributable to common stockholders - Basic	22,798,048	7,912,172	13,646,814	7,753,571
Effect of dilutive stock option	2,840,161			
Effect of dilutive RSU and RSA	311,314			
Effect of dilutive ESPP and warrant	122,006			
Weighted average shares used in computing net income (loss) per share attributable to common stockholders - Diluted	26,071,528	7,912,172	13,646,814	7,753,571
Net income (loss) per share attributable to common stockholders				
Basic	$ 0.07	$ (0.16)	$ (0.12)	$ (0.78)
Diluted	$ 0.06	$ (0.16)	$ (0.12)	$ (0.78)

7. Geographic Information

The Company has one operating segment with one business activity developing and monetizing revenue management solutions.

Revenues from External Customers

Revenues from customers outside the United States were 14% and 11% of total revenues for the three months and nine months ended June 30, 2013, respectively. Revenues from customers outside the United States were less than 10% of total revenues for both the three months and nine months ended June 30, 2012.

Long-Lived Assets

The following table sets forth the Company s property and equipment, net by geographic region:

	As of June 30, 2013	As of September 30, 2012
	(in thousands)	
United States	$ 5,887	$ 3,335
Other	1,026	1,255
Total property and equipment, net	$ 6,913	$ 4,590

Table of Contents

8. Acquisition

On January 18, 2012, the Company acquired certain assets of LeapFrogRx, a privately held cloud-based analytics solution provider for the pharmaceutical industry. The Company paid total purchase consideration of $3.0 million in cash.

The purchase price was allocated to tangible and identifiable intangible assets acquired and liabilities assumed based on their respective estimated fair values on the date of acquisition. The purchase accounting allocation resulted in intangible assets of $1.5 million and goodwill of $1.2 million. Intangible assets acquired included developed technology, backlog, non-competition agreements and customer relationships, and are being amortized on a straight-line basis over their estimated useful lives of 3 to 5 years. The key factors attributable to the creation of goodwill by the transaction are synergies in skill-sets, operations, customer base and organizational cultures.

The allocation of the purchase price was as follows:

	Amount (in thousands)
Tangible assets	$ 685
Intangible assets:	
Developed technology	1,124
Backlog	100
Non-competition agreements	100
Customer relationships	158
Liabilities assumed	(1,024)
Payments due from seller	667
Goodwill	1,190
Total purchase price	$ 3,000

Retention-Related Payments

In addition to the total purchase consideration of $3.0 million, the Company is contingently obligated to make additional payments, as described below, which are expected to be incurred through January 2015. These cash payments are subject to future employment and are considered compensatory in nature and are being recognized as compensation expense.

The Company made payments of $3.0 million in July 2012 and $1.0 million in January 2013. Additionally, payments of $1.0 million are due on each of January 2014 and 2015. Due to the employment service criteria associated with these payments, expenses are being recognized ratably over the term of each payment beginning from the date of the acquisition. The Company recognized compensation expenses of $0.2 million and $0.9 million for the three months and nine months ended June 30, 2013, respectively. The Company recognized compensation expenses of $2.0 million and $3.6 million for the three months and nine months ended June 30, 2012.

In addition, up to $1.0 million of earn-out consideration is payable based on revenue recognized during the twelve-month period January 2014. Due to the employment service criteria associated with these payments, expenses are being recognized ratably over the term of each payment beginning from the date of acquisition. The Company recognized zero for the three months ended June 30, 2013 and recognized a credit of $0.3 million for the nine months ended June 30, 2013, respectively. The Company recognized expenses of $0.1 million and $0.2 million for the three months and nine months ended June 30, 2012, respectively.

The Company paid one-time retention bonus amounts to the former employees of LeapFrogRx totaling $0.3 million in January 2013 and guaranteed bonus payments totaling $0.4 million for the fiscal year ended September 30, 2012 that were subject to continuous employment. In addition, the Company issued 200,000 shares of restricted stock to certain employees of LeapFrogRx (see Note 4).

Included in the Company s condensed consolidated statement of operations for the three months and nine months ended June 30, 2012, are revenues of approximately $2.3 million and $3.9 million from LeapFrogRx since its acquisition in January 2012.

Pro Forma Results

Pro forma results assuming that the acquisition had occurred as of October 1, 2010 would have resulted in total revenues and a net loss of $64.4 million and $6.2 million, respectively, for the nine months ended June 30, 2012.

Table of Contents

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

This report contains forward-looking statements regarding future events and our future results that are subject to the safe harbors created under the Securities Act of 1933 (Securities Act) and the Securities Exchange Act of 1934 (Exchange Act). All statements other than statements of historical facts are statements that could be deemed forward-looking statements. These statements are based on current expectations, estimates, forecasts, and projections about the industries in which we operate and the beliefs and assumptions of our management. Words such as anticipates, goals, plans, believes, seeks, estimates, continues, may, will, variations of such words and similar expressions are int identify such forward-looking statements. In addition, any statements that refer to projections of our future financial performance, our anticipated growth and trends in our businesses, and other characterizations of future events or circumstances are forward-looking statements. You should not rely upon forward-looking statements as predictions of future events. The events and circumstances reflected in the forward-looking statements may not be achieved or occur. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, or achievements. Forward-looking statements are based only on our current expectations and projections and are subject to risks, uncertainties, and assumptions that are difficult to predict, including those identified below under Part II, Item 1A. Risk Factors, and elsewhere in this report. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. We undertake no obligation to revise or update any forward-looking statements for any reason.

As used in this report, the terms we, us, our, and the Company mean Model N, Inc. and its subsidiaries unless the context indicates otherwise.

Overview

We are a provider of revenue management solutions for the life science and technology industries. Our solutions enable our customers to maximize revenues and reduce revenue compliance risk by transforming their revenue lifecycle from a series of tactical, disjointed operations into a strategic end-to-end process. We believe our solutions serve as the system of record for our customers revenue management processes and can provide a competitive advantage for them.

Our solutions are comprised of two complementary suites of software applications: Revenue Management Enterprise and Revenue Management Intelligence. Sales of our solutions range from individual applications to complete suites, and deployments may vary from specific divisions or territories to enterprise-wide implementations.

We derive revenues primarily from the sale of our on-premise and cloud-based solutions and related implementation services, as well as maintenance and support and application support. We price our solutions based on a number of factors, including revenues under management and number of users. Our license and implementation revenues are comprised of sales of perpetual license and related implementation services, which revenues are recognized over the implementation period, which commences when implementation work begins and typically ranges from a few months to three years. Maintenance and support revenues are recognized ratably over the support period, which is typically one year. SaaS revenues for cloud-based solutions are derived from subscription fees from customers accessing our cloud-based solutions, as well as from associated implementation services. The actual timing of revenue recognition may vary based on our customers implementation requirements and availability of our services personnel.

We market and sell our solutions to customers in the life science and technology industries. While we have historically generated the substantial majority of our revenues from companies in the life science industry, we have also grown our base of technology customers and intend to continue to focus on increasing the revenues from customers in the technology industry. Our most significant customers in any given period generally vary from period to period due to the timing of implementation and related revenue recognition over those periods of larger projects.

For the three months ended June 30, 2013 and 2012, our revenues were $27.2 million and $22.8 million, respectively, representing year-over-year growth of approximately 20%. We recently experienced challenges in sales execution and our ability to maintain this growth rate throughout our 2014 fiscal year will depend on how quickly we can strengthen this area. For the three months ended June 30, 2013, approximately 14% of our revenues were derived from customers located outside the United States.

Table of Contents

Key Business Metrics

In addition to the measures of financial performance presented in our consolidated financial statements, we use certain key metrics to evaluate and manage our business, including four-quarter revenues from current customers and Adjusted EBITDA. We use these key metrics internally to manage the business, and we believe they are useful for investors to compare key financial data from various periods.

Four-Quarter Revenues From Existing Customers

We derive a large majority of revenues from existing customers, which we define as customers from which we have generated revenues in each of the preceding four quarters, which would exclude historical customers of LeapFrogRx. We measure four-quarter revenues from our existing license and subscription customers by calculating the sum of revenues recognized during the last four quarters from any customer that has contributed revenue in each of the preceding four quarters. We believe four-quarter revenues from existing customers provides us and investors with a metric to measure the historical revenue visibility in our business. We also use this metric internally to understand the proportion of revenues being generated in any period from existing customers as compared to entirely new customers or customers with whom we have not been recently engaged. This measure helps us guide our sales activities and establish budgets and operational goals for our sales function.

Our four-quarter revenues from existing customers for the periods presented were as follows:

	Four Quarters Ended (unaudited) (in thousands)					
	March 31, 2012	June 30, 2012	September 30, 2012	December 31, 2012	March 31, 2013	June 30, 2013
Four-quarter revenues	$ 66,785	$ 73,157	$ 76,892	$ 77,633	$ 82,956	$ 85,856

Non-GAAP Financial Measure

Adjusted EBITDA

Adjusted EBITDA is a financial measure that is not calculated in accordance with generally accepted accounting principles in the United States (U.S. GAAP). We define Adjusted EBITDA as net loss before LeapFrogRx compensation charges, as discussed below, stock-based compensation, depreciation and amortization, interest expense, net, other income (expenses), net, and provision for income taxes. We believe Adjusted EBITDA provides investors with consistency and comparability with our past financial performance and facilitates period-to-period comparisons of our operating results and our competitors operating results. We also use this measure internally to establish budgets and operational goals to manage our business and evaluate our performance.

We understand that, although Adjusted EBITDA is frequently used by investors and securities analysts in their evaluations of companies, Adjusted EBITDA has limitations as an analytical tool, and it should not be considered in isolation or as a substitute for analysis of our results of operations as reported under U.S. GAAP. These limitations include:

Adjusted EBITDA does not include the effect of the LeapFrogRx compensation charges, which are a cash expense;

Adjusted EBITDA does not reflect stock-based compensation expense;

Depreciation and amortization are non-cash charges, and the assets being depreciated or amortized will often have to be replaced in the future; Adjusted EBITDA does not reflect any cash requirements for these replacements;

Adjusted EBITDA does not reflect cash requirements for income taxes and the cash impact of other income or expense; and

Other companies in our industry may calculate Adjusted EBITDA differently than we do, limiting its usefulness as a comparative measure.

Table of Contents

The following tables provide a reconciliation of Adjusted EBITDA to net income (loss):

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2013	2012	2013	2012
	(in thousands)			
Reconciliation of Adjusted EBITDA:				
Net income (loss)	$ 1,535	$ (1,236)	$ (1,674)	$ (6,066)
Adjustments:				
LeapFrogRx compensation charges	200	2,144	614	3,933
Stock-based compensation	1,807	411	3,306	2,005
Depreciation and amortization	559	462	1,661	1,234
Interest expense, net	85	160	326	514
Other (income) expenses, net	(48)	(36)	664	549
Provision for income taxes	81	92	230	231
Adjusted EBITDA	$ 4,219	$ 1,997	$ 5,127	$ 2,400

Adjusted EBITDA was $4.2 million, $2.0 million, $5.1 million and $2.4 million for the three months ended June 30, 2013 and 2012 and nine months ended June 30, 2013 and 2012, respectively. Our Adjusted EBITDA for the three and nine months ended June 30, 2013 increased primarily due to increases in total revenues, which were partially offset by increased expenses. The increase in expenses was primarily due to increases in personnel costs arising principally from headcount increases and increased use of third-party contractors.

Key Components of Results of Operations

Revenues

Revenues are comprised of license and implementation revenues and SaaS and maintenance revenues.

License and Implementation

License and implementation revenues are generated from the sale of software licenses for our on-premise solutions and related implementation services.

SaaS and Maintenance

SaaS and maintenance revenues primarily include subscription and related implementation fees from customers accessing our cloud-based solutions and revenues associated with maintenance contracts from license customers. Also included in SaaS and maintenance revenues are other revenues, including revenues related to application support, training and customer-reimbursed expenses. Prior to 2012, revenues from subscriptions for our cloud-based solutions were not material; however, following our acquisition of LeapFrogRx in January 2012, they have increased but remain less than 15% of our total revenues. Over time, we expect that SaaS revenues will increase as a percentage of total revenues.

Cost of Revenues

Our total cost of revenues is comprised of the following:

License and Implementation

Cost of license and implementation revenues includes costs related to the implementation of our on-premise solutions. Cost of license and implementation revenues primarily consists of personnel-related costs including salary, bonus, stock-based compensation and overhead allocation as well as third-party contractors, royalty fees paid to third parties for rights to their intellectual property and travel-related expenses. Cost of license and implementation revenues may vary from period to period depending on a number of factors, including the amount of implementation services required to deploy our solutions and the level of involvement of third-party contractors providing implementation services.

SaaS and Maintenance

Cost of SaaS and maintenance revenues includes those costs related to the implementation of our cloud-based solutions, maintenance and support and application support for our on-premise solutions and training. Cost of SaaS and maintenance revenues primarily consists of personnel-related costs including salary, bonus, stock-based compensation, LeapFrogRx compensation charges and overhead allocation as well as reimbursable expenses, third-party contractors and data center-related expenses. We believe that cost of SaaS and maintenance revenues will continue to increase in absolute dollars as we continue to focus on building infrastructure for our cloud-based solutions.

Operating Expenses

Our operating expenses consist of research and development, sales and marketing and general and administrative expenses.

Research and Development

Our research and development expenses consist primarily of personnel-related costs including salary, bonus, stock-based compensation and overhead allocation as well as third-party contractors and travel-related expenses. Our software development costs for new software solutions and enhancements to existing software solutions are generally expensed as incurred. However, we capitalize development costs incurred in connection with the development of certain additional service offerings that will only be offered through the cloud. We expect to cease capitalization of development costs when we have completed all final testing of this product, at which time amortization charges related to such capitalized costs will be included in cost of revenues. As of June 30, 2013, we had $4.0 million of capitalized software development costs. We have not begun to amortize any of these capitalized software development costs as the development of the product is not completed. We expect our research and development expenses to increase in absolute dollars as we continue to develop new applications and enhance our existing software solutions.

Sales and Marketing

Our sales and marketing expenses consist primarily of personnel-related costs including salary, bonus, commissions, stock-based compensation, and overhead allocation as well as third-party contractors, travel-related expenses and marketing programs. We recognize sales commission expense upon contract signing, while we recognize revenue over the period the services are provided. We expect our sales and marketing expenses to increase in absolute dollars as we increase the number of our sales and marketing employees to support the growth in our business.

General and Administrative

Our general and administrative expenses consist primarily of personnel-related costs including salary, bonus, stock-based compensation, and overhead allocation, audit and legal fees as well as third-party contractors and travel-related expenses. We expect to incur significant additional accounting and legal costs related to being a public company, as well as additional insurance, investor relations and other costs. In addition, we expect to incur additional costs related to the implementation of a new enterprise resource planning (ERP) system.

LeapFrogRx Compensation Charges

In January 2012, we acquired LeapFrogRx for initial cash consideration of $3.0 million as well as potential additional payments to former LeapFrogRx stockholders totaling up to $8.3 million, which are expected to be incurred through January 2015. These additional payments are, among other things, subject to future continued employment and are therefore considered compensatory in nature and are being recognized as compensation expense (LeapFrogRx compensation charges) over the term of each component. As of June 30, 2013, we had expensed an aggregate of $5.5 million of LeapFrogRx compensation charges.

Table of Contents

Results of Operations

The following tables set forth our consolidated results of operations for the periods presented and as a percentage of our total revenues for those periods. The period-to-period comparison of financial results is not necessarily indicative of financial results to be achieved in future periods.

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2013	2012	2013	2012
	(in thousands)			
Revenues:				
License and implementation	$ 16,419	$ 13,191	$ 43,362	$ 36,215
SaaS and maintenance	10,828	9,582	30,785	24,855
Total revenues	27,247	22,773	74,147	61,070
Cost of Revenues:				
License and implementation[1]	7,527	5,712	19,887	16,255
SaaS and maintenance[1]	4,865	5,616	14,169	13,280
Total cost of revenues	12,392	11,328	34,056	29,535
Gross profit	14,855	11,445	40,091	31,535
Operating Expenses:				
Research and development[1]	4,063	4,491	12,665	13,481
Sales and marketing[1]	5,256	5,356	16,362	15,042
General and administrative[1]	3,883	2,618	11,518	7,784
Total operating expenses	13,202	12,465	40,545	36,307
Income (loss) from operations	1,653	(1,020)	(454)	(4,772)
Interest expense, net	85	160	326	514
Other (income) expenses, net	(48)	(36)	664	549
Income (loss) before income taxes	1,616	(1,144)	(1,444)	(5,835)
Provision for income taxes	81	92	230	231
Net income (loss)	$ 1,535	$ (1,236)	$ (1,674)	$ (6,066)

(1) Includes stock-based compensation as follows:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2013	2012	2013	2012
Cost of services:				
License and implementation	$ 240	$ 61	$ 370	$ 207
SaaS and maintenance	215	77	403	469
Research and development	305	56	457	226
Sales and marketing	686	167	1,399	941
General and administrative	361	50	677	162
Total stock-based compensation	$ 1,807	$ 411	$ 3,306	$ 2,005

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2013	2012	2013	2012
	(as of % of revenues)			
Revenues:				
License and implementation	60%	58%	58%	59%
SaaS and maintenance	40	42	42	41
Total revenues	100	100	100	100
Cost of Revenues:				

License and implementation	27	25	27	26
SaaS and maintenance	18	25	19	22
Total cost of revenues	45	50	46	48
Gross profit	55	50	54	52
Operating Expenses:				
Research and development	15	20	17	22
Sales and marketing	20	24	22	25
General and administrative	14	11	16	13
Total operating expenses	49	55	55	60
Income (loss) from operations	6	(5)	(1)	(8)
Interest expense, net				1
Other (income) expenses, net			1	1
Income (loss) before income taxes	6	(5)	(2)	(10)
Provision for income taxes				
Net income (loss)	6%	(5)%	(2)%	(10)%

Table of Contents

Comparison of the Three Months Ended June 30, 2013 and 2012

Revenues

	Three Months Ended June 30,					
	2013		2012		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	($)	(%)
	(in thousands, except percentages)					
Revenues:						
License and implementation	$ 16,419	60%	$ 13,191	58%	$ 3,228	24%
SaaS and maintenance	10,828	40	9,582	42	1,246	13
Total revenues	$ 27,247	100%	$ 22,773	100%	$ 4,474	20

License and Implementation

License and implementation revenues increased by $3.2 million, or 24%, to $16.4 million for the three months ended June 30, 2013 from $13.2 million for the three months ended June 30, 2012. Our revenues from existing customers were $13.2 million for the three months ended June 30, 2013 and $9.6 million for the three months ended June 30, 2012. The increase was primarily due to an increase in sales volume.

SaaS and Maintenance

SaaS and maintenance revenues increased by $1.2 million, or 13%, to $10.8 million for the three months ended June 30, 2013 from $9.6 million for the three months ended June 30, 2012. The increase in SaaS and maintenance revenues was primarily due to an increase in maintenance and support, and application support revenues of $0.9 million due to an increase in the number of service contracts and an increase in SaaS and related implementation revenues of $0.2 million.

Cost of Revenues

	Three Months Ended June 30,					
	2013		2012		Change	
	Amount	% of Revenues	Amount	% of Revenues	($)	(%)
	(in thousands, except percentages)					
Cost of revenues:						
License and implementation	$ 7,527	27%	$ 5,712	25%	$ 1,815	32%
SaaS and maintenance	4,865	18	5,616	25	(751)	(13)
Total cost of revenues	$ 12,392	45	$ 11,328	50	$ 1,064	9
Gross profit:						
License and implementation	$ 8,892	33%	$ 7,479	33%	$ 1,413	19%
SaaS and maintenance	5,963	22	3,966	17	1,997	50
Total gross profit	$ 14,855	55	$ 11,445	50	$ 3,410	30

License and Implementation

Cost of license and implementation revenues increased by $1.8 million, or 32%, to $7.5 million during the three months ended June 30, 2013 from $5.7 million for the three months ended June 30, 2012. The increase in the cost of license and implementation revenues was primarily due to additional in-house personnel as well as third-party contractors deployed in the professional services group.

SaaS and Maintenance

Cost of SaaS and maintenance revenues decreased by $0.8 million, or 13%, to $4.9 million during the three months ended June 30, 2013 from $5.6 million for the three months ended June 30, 2012. The decrease in the cost of SaaS and maintenance revenues was primarily the result of a decrease in LeapFrogRx compensation charge of $1.1 million, partially offset by an increase in personnel costs and third-party contractors charges of $0.3 million.

Table of Contents

Operating Expenses

	Three Months Ended June 30, 2013 Amount	2012 Amount	Change ($)	(%)
	(in thousands, except percentages)			
Operating expenses:				
Research and development	$ 4,063	$ 4,491	$ (428)	(10)%
Sales and marketing	5,256	5,356	(100)	(2)
General and administrative	3,883	2,618	1,265	48
Total operating expenses	$ 13,202	$ 12,465	$ 737	6

Research and Development

Research and development expenses decreased by $0.4 million, or 10%, to $4.1 million during the three months ended June 30, 2013 as compared to $4.5 million for the three months ended June 30, 2012. The decrease was the result of an increase in expenses allocated to cost of revenues for time spent on revenue generating projects of $0.7 million, partially offset by an increase in stock-based compensation of $0.3 million. We believe that continued investment in our technology is important to our future growth, and as a result, we expect research and development expenses to increase in absolute dollars in the future.

Sales and Marketing

Sales and marketing expenses during the three months ended June 30, 2013 were relatively consistent with sales and marketing expenses for the three months ended June 30, 2012. We expect sales and marketing expenses to increase in absolute dollars in the future as we continue to expand our direct sales teams and increase our marketing activities.

General and Administrative

General and administrative expenses increased by $1.3 million, or 48%, to $3.9 million during the three months ended June 30, 2013 as compared to $2.6 million for the three months ended June 30, 2012. This increase was primarily due to an increase in personnel costs of $0.5 million due to the increase in headcount and an increase in stock-based compensation of $0.3 million. We expect to incur higher general and administrative expenses in absolute dollars as a result of both our growth and our being a public company, including higher legal, insurance and accounting expenses.

Interest and Other Expense, Net

	Three Months Ended June 30, 2013 Amount	2012 Amount	Change ($)	(%)
	(in thousands, except percentages)			
Interest expense, net	$ 85	$ 160	$ (75)	(47)%
Other (income) expenses, net	(48)	(36)	(12)	33

Interest expense, net primarily relates to financing costs related to our term loan and capital leases. The decrease was primarily due to the repayment in full of our term loan in May 2013.

Other (income) expenses, net during the three months ended June 30, 2013 were relatively consistent with other (income) expenses, net for the three months ended June 30, 2012.

Provision for Income Taxes

	Three Months Ended June 30,			
	2013	2012	Change	
	Amount	Amount	($)	(%)
	(in thousands, except percentages)			
Provision for income taxes	$ 81	$ 92	$ (11)	(12)%

Provision for income taxes is primarily related to the state minimum tax and foreign tax on our profitable foreign operations. The change in income tax provision is primarily due to the change in income related to our foreign operations.

Table of Contents

Comparison of the Nine Months Ended June 30, 2013 and 2012

Revenues

	Nine Months Ended June 30, 2013		2012		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	($)	(%)
	(in thousands, except percentages)					
Revenues:						
License and implementation	$ 43,362	58%	$ 36,215	59%	$ 7,147	20%
SaaS and maintenance	30,785	42	24,855	41	5,930	24
Total revenues	$ 74,147	100%	$ 61,070	100%	$ 13,077	21

License and Implementation

License and implementation revenues increased by $7.1 million, or 20%, to $43.3 million for the nine months ended June 30, 2013 from $36.2 million for the nine months ended June 30, 2012. Our revenues from existing customers were $36.8 million for the nine months ended June 30, 2013 and $28.4 million for the nine months ended June 30, 2012. The increase was primarily due to an increase in sales volume.

SaaS and Maintenance

SaaS and maintenance revenues increased by $5.9 million, or 24%, to $30.8 million for the nine months ended June 30 from $24.9 million for the nine months ended June 30, 2012. The increase in SaaS and maintenance revenues was primarily due to an increase in SaaS and related implementation revenues of $4.1 million and an increase in maintenance and application support revenues of $2.1 million due to an increase in the number of service contracts.

Cost of Revenues

Nine Months Ended
June 30,