MARIN SOFTWARE INC
Form 10-K
February 20, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x **Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the fiscal year ended December 31, 2014

OR

¨ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
Commission File Number: 001-35838

Marin Software Incorporated

(Exact name of registrant as specified in its charter)

Delaware	**20-4647180**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

123 Mission Street, 25th Floor

San Francisco, CA 94105

(415) 399-2580

(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common stock, par value $0.001 per share	**New York Stock Exchange**

Securities registered pursuant to section 12(g) of the Act:

Not applicable

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of Act. Yes ¨ No x

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 check mark 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

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

Based on the closing price of the Registrant s Common Stock on the New York Stock Exchange of $11.77 on the last business day of the Registrant s most recently completed second fiscal quarter, which was June 30, 2014, the aggregate market value of its shares held by non-affiliates was approximately $229 million. Shares of the Registrant s Common Stock held by each executive officer and director and by each entity or person that owned 5 percent or more of the Registrant s outstanding Common Stock were excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of January 31, 2015, there were approximately 35.4 million shares of the Registrant s Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s definitive proxy statement for its 2015 Annual Meeting of Stockholders (the Proxy Statement), to be filed within 120 days of the Registrant s fiscal year ended December 31, 2014, are incorporated by reference in Part III of this Report on Form 10-K. Except with respect to information specifically incorporated by reference in this Form 10-K, the Proxy Statement is not deemed to be filed as part of this Form 10-K.

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MARIN SOFTWARE INCORPORATED

FORM 10-K

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K, including the Management s Discussion and Analysis of Financial Condition and Results of Operations, 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 and the Securities Exchange Act of 1934. All statements contained in this Annual Report on Form 10-K other than statements of historical fact, including statements regarding our future results of operations and financial position, our business strategy and plans, and our objectives for future operations, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words believe, may, potentially, will, estimate, continue, anticipate, intend, could, wo expect, seek, and similar expressions are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations, estimates and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs. These statements reflect our beliefs and certain assumptions based upon information available to us at the time we file this Annual Report on Form 10-K or the time of the documents incorporated by reference. Such forward-looking statements are only predictions, which may differ materially from actual results or future events. Although we believe that our expectations, estimates and projections reflected in the forward-looking statements are reasonable, we cannot be sure that they will be achieved. These forward-looking statements are subject to a number of risks, uncertainties and assumptions, including those described in the Risk Factors section. Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the future events and trends discussed in this report may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward-looking statements. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements, except as required by law. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

As used in this report, the terms Marin, Registrant, we, us, our, and the Company mean Marin Software Inco and its subsidiaries unless the context indicates otherwise.

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PART I

ITEM 1. BUSINESS

We provide a leading cross-channel advertising cloud platform that enables digital marketers to improve performance of their online advertising campaigns, realize efficiencies and time savings, and make better business decisions.

Our integrated platform is a software-as-a-service (SaaS) analytics, workflow and optimization solution for marketing professionals, allowing them to effectively manage their digital advertising spend across search, display, social and mobile advertising channels. Our software solution is designed to help our customers:

- measure the effectiveness of their advertising campaigns through our proprietary reporting and analytics capabilities;
- manage and execute campaigns through our intuitive user interface and underlying technology that streamlines and automates key functions, such as ad creation and bidding, across multiple publishers and channels; and
- optimize campaigns across multiple publishers and channels in real time based on market and business data to achieve desired revenue outcomes using our predictive bid management technology.

Advertisers use our platform to create, target and convert precise audiences based on recent buying signals from users search, social and display interactions. Our platform is integrated with leading publishers such as Baidu, Bing, Facebook, Google, Twitter, Yandex, Yahoo! and Yahoo! Japan. Additionally, we have integrations with more than 45 leading web analytics and ad-serving solutions and key enterprise applications, enabling our customers to more accurately measure the return on investment of their marketing programs.

Our software platform serves as an integration point for advertising performance, sales and revenue data, allowing advertisers to connect the dots between advertising spend and revenue outcomes. Through an intuitive interface, we enable our customers to simultaneously run large-scale digital advertising campaigns across multiple publishers and channels, making it easy for marketers to create, publish, modify and optimize campaigns in real time.

Our predictive bid management and optimization technology also allows advertisers to forecast outcomes and optimize campaigns across multiple publishers and channels to achieve their business goals. Our optimization technology can help advertisers increase ad spend on those campaigns, publishers and channels that are performing well while reducing investment in those that are not. This category of solutions, which we refer to as cross-channel bid and campaign optimization, helps businesses intelligently and efficiently measure, manage, and optimize their digital advertising spend to achieve desired business results.

We completed our acquisition of NowSpots, Inc., which conducted business as Perfect Audience (Perfect Audience), in June 2014 to complement our offered solutions. Perfect Audience offers advertisers a SaaS demand-side platform to purchase display impressions and retarget audiences across the web, Facebook and Twitter. With the acquisition, we expanded our cross-channel capabilities by adding new programmatic display and social advertising functions while expanding our audience retargeting tools. This acquisition is more fully described in Note 3 to the Consolidated

Financial Statements. In February 2015 we completed the acquisition of SocialMoov, a Paris-based company, which is a social advertising software platform for Facebook and Twitter advertisers. SocialMoov offers advertisers and agencies novel social advertising tools designed to increase engagement and return on investment. This acquisition will provide us with innovative social advertising technologies, including Facebook video advertising, Twitter application program interface (API) integration and television synchronization, which will augment our current social offering.

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Headquartered in San Francisco, we were founded in 2006. The mailing address of our headquarters is 123 Mission Street, 25th Floor, San Francisco, California 94105 and our telephone number at that location is (415) 399-2580. As of December 31, 2014, our customers collectively managed more than $7.2 billion in annualized ad spend on our platform, which we believe makes us the largest offeror of independent advertising cloud solutions.

Offered Solutions

Our cloud-based platform helps our customers to measure, manage and optimize their digital marketing campaigns to improve performance of their online advertising campaigns, realize efficiencies and time savings, and make better business decisions. We currently offer two editions of our search platform that leverage the same underlying technology.

Enterprise Edition. Targeting large advertisers and agencies, *Marin Enterprise* is designed to provide digital advertisers with the power, scale and flexibility required to manage large-scale advertising campaigns.

Professional Edition. Targeting mid-market advertisers and agencies, *Marin Professional* is designed for rapid deployment and offers customers a complete workflow, analysis and optimization solution for managing digital advertising.

Our software platform is comprised of the following modules:

Optimization. Our *Optimization* functionalities help advertisers manage bids across publishers to meet revenue goals and identify opportunities for campaign improvements leading to improved financial performance and efficiencies.

Reporting and Analytics. Our *Reporting and Analytics* module enables advertisers to report results at a business level and analyze cross-channel performance trends, leading to improved visibility and significant time savings.

Campaign Management. Our *Campaign Management* module provides the digital advertiser with a unified interface to create, manage and optimize campaigns across a broad range of publishers, leading to greater efficiencies and increased flexibility.

Connect. Our *Connect* family of products enables advertisers automate and streamline their ability to capture revenue, cost and audience data from a range of sources such as ad servers, analytics systems, CRM platforms, publishers and third party databases. Through integrations across multiple data sources, our *Connect* module can assist advertisers in having a holistic picture of their digital advertising campaigns.

Technology & Supporting Platform

We designed our cloud-based platform to support large global advertisers. The majority of our software is written in Java. Our hardware consists of industry-standard servers and network infrastructure. Our standard operating system is

Linux. Our software platform is character-set, language, currency, and time-zone independent. Our technology platform has the following key benefits:

Scalability. Our software platform is designed to handle billions of ad units across thousands of advertisers, while delivering a responsive browsing and editing experience. As the number of advertisers and resulting computing and storage requirements grow, we can add hardware to our platform to accommodate growing demand.

Availability. Our customers are highly dependent on the availability of our platform, which is designed to be available 24x7, 365 days a year. We operate our own hardware and use third-party data centers that offer server redundancy, back-up communications and power and physical security.

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Security. Our software platform manages a large quantity of customer data. We employ technologies, policies and procedures to protect customer data. Our primary third-party data center has SSAE 16 attestations.

Customers

We market and sell our solutions to advertisers directly and through advertising agencies that use our platform on behalf of their customers. Advertisers that we serve through our relationships with agencies have historically represented about half our revenues. There were no customers that accounted for greater than 10% of our revenues in 2014, 2013 or 2012.

Competition

The digital advertising platform market is highly competitive, fragmented, and subject to changes in both technology and customer behavior. We face significant competition today and expect competition to intensify in the future. To maintain and improve our competitive position, we must keep pace with the evolving needs of our customers and continue to develop and introduce new modules, features and services in a timely and efficient manner. We currently compete with large, well-established companies, such as Adobe Systems Incorporated and Google Inc. (through its wholly-owned subsidiary DoubleClick), and privately-held companies, such as Kenshoo Ltd. We also compete with in-house proprietary tools, tools from publishers and custom solutions, including spreadsheets. We believe the principal competitive factors in our market include the following:

- solution quality, breadth, flexibility and functionality;
- tangible platform benefits;
- level of customer satisfaction and our ability to respond to customer needs rapidly;
- breadth and quality of advertiser and agency relationships;
- ability to innovate and develop new or improved products and modules;
- ability to respond to changes in publishers APIs;
- brand awareness and reputation; and
- size of customer base.

Apart from cross-channel platform competitors, we also compete with channel solutions in display and social. Competitors in display include public companies such as Criteo S.A. and Rocket Fuel Inc., as well as privately-held companies such as AdRoll Inc. and MediaMath Inc., while in social we compete with public companies such as

Salesforce.com (through its wholly-owned subsidiary Social.com), and privately-held companies such as Nanigans, Inc.

Our ability to remain competitive will largely depend on our ongoing performance in the areas of our solution breadth and depth as well as customer support.

Sales and Marketing

We sell our solutions directly to advertisers and to agencies in a wide range of industries through our global sales team. Our sales cycle can vary substantially by advertiser and agency, but typically is one to nine months. We have a number of account executive sales teams organized by geography and market segments. We also have Customer Success professionals who are responsible for long-term customer satisfaction and retention, renewal, and driving an increase in the volume of media managed by customers on our platform.

Our marketing team is focused on driving awareness and demand generation across major markets. This team provides thought leadership in the form of white papers, benchmarking reports, bylines, presenting at industry conferences and speaking to the press. In addition, they are responsible for the creation of field enablement assets such as case studies, blog posts and corporate and product collateral.

Research and Development

Our research and development team is responsible for the design, development, and maintenance of our platform. Our research and development process emphasizes frequent, iterative and incremental development cycles. Within our research and development organizations, we have several project teams that focus on platform and feature development for our integrated vertical offerings as part of our Ad Cloud solutions. Each of these project teams includes engineers, quality engineers and product managers, as needed, responsible for the initial and ongoing development for their projects. Total research and development expense was $28.8 million, $20.7 million and $14.0 million and for the years ended December 31, 2014, 2013 and 2012.

Employees

As of December 31, 2014, we had a total of 571 regular full-time employees, including 170 employees located outside the United States. None of our employees are represented by a labor union or covered by a collective bargaining agreement. We have not experienced any work stoppages, and we consider our relations with our employees to be good.

Intellectual Property

Our intellectual property rights are a key component of our success. We rely on a combination of patent, trademark, copyright, unfair competition and trade secret laws, as well as confidentiality procedures and contractual restrictions, to establish, maintain and protect our proprietary rights.

As of December 31, 2014, we had two issued patents and five patent applications pending in the United States.

We own and use trademarks on or in connection with our products and services, including one trademark registered with the European Union and Australia and unregistered common law marks and pending trademark applications in the United States, China, Japan and Singapore. We have also registered numerous Internet domain names.

Available Information

The mailing address of our headquarters is 123 Mission Street, 25th Floor, San Francisco, California 94105 and our telephone number at that location is (415) 399-2580. Our website is www.marinsoftware.com. Through a link on the Investor Center section of our website, we make available the following filings as soon as reasonably practicable after they are electronically filed with or furnished to the Securities and Exchange Commission (the SEC): our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934. All such filings are free of charge. The information posted to our website is not incorporated into this Annual Report on Form 10-K. The public may read and copy any materials that we file with the SEC at the SEC s Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at www.sec.gov.

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ITEM 1A. RISK FACTORS

Our operations and financial results are subject to various risks and uncertainties, including those described below, which could adversely affect our business, results of operations, cash flows, financial conditions, and the trading price of our common stock.

Risks Related to Our Business

We have a history of losses and we may not achieve or sustain profitability in the future.

We have incurred significant losses in each fiscal year since our incorporation in 2006. We experienced net losses of $33.2 million during 2014. As of December 31, 2014, we had an accumulated deficit of $146.4 million. The losses and accumulated deficit were due to the substantial investments we made to grow our business and acquire customers. We anticipate that our cost of revenues and operating expenses will increase in the foreseeable future as we continue to invest to grow our business and acquire customers and develop our platform and new functionality. These efforts may prove more expensive than we currently anticipate, and we may not succeed in increasing our revenues sufficiently to offset these higher expenses. Many of our efforts to generate revenues from our business are new and unproven, and any failure to increase our revenues or generate revenues from new solutions could prevent us from attaining or increasing profitability. Furthermore, to the extent we are successful in increasing our customer base, we also could incur increased losses because costs associated with entering into customer contracts are generally incurred up front, while customers are billed over the term of the contract generally through our usage-based pricing model. We do not expect to be profitable in 2015 on the basis of generally accepted accounting principles in the United States (GAAP) and we cannot be certain that we will be able to attain profitability on a quarterly or annual basis, or if we do, that we will sustain profitability.

Our limited operating history makes it difficult to evaluate our current business and future prospects.

Although we began our operations in March 2006, we did not begin generating substantial revenues until 2009. Our limited operating history may make it difficult to evaluate our current business and our future prospects. We have encountered and will continue to encounter risks and difficulties frequently experienced by growing companies in rapidly developing and changing industries, including challenges in forecasting accuracy, hiring and retaining qualified employees, determining appropriate investments of our limited resources, market acceptance of our existing and future solutions, competition from established companies with greater financial and technical resources, acquiring and retaining customers, managing customer deployments and developing new solutions. Our current operations infrastructure may require changes in order for us to achieve profitability and scale our operations efficiently. For example, we may need to automate portions of our solution to decrease our costs, ensure our marketing infrastructure is designed to drive highly qualified leads cost effectively and implement changes in our sales model to improve the predictability of our sales and reduce our sales cycle. If we fail to implement these changes on a timely basis or are unable to implement them due to factors beyond our control, our business may suffer, our revenue may decline and we may not be able to achieve further growth or profitability. We cannot assure you that we will be successful in addressing these and other challenges we may face in the future.

Our usage-based pricing model makes it difficult to forecast revenues from our current customers and future prospects.

We primarily have a usage-based pricing model in which most of our fees are calculated as a percentage of customers advertising spend managed on our platforms. This pricing model makes it difficult to accurately forecast revenues because our customers advertising spend managed by our platforms may vary from month to month based on the variety of industries in which our advertisers operate, the seasonality of those industries and fluctuations in our customers advertising budgets or other factors. Our contracts with our direct advertiser customers generally contain a minimum monthly fee, which is generally greater than one-half of our estimated monthly revenues from the customer at the time the contract is signed, and, as a result, the monthly minimum may not be a good indicator of our revenues from that customer. In addition, advertisers that use our platform through our agency customers typically do not have a minimum monthly spend amount or a minimum term during which they must use our platform and, as a result, the ability to forecast revenues from these advertisers is difficult. If we incorrectly forecast revenues for these advertisers and the amount of revenue is less than projections we provide to investors, the price of our common stock could decline substantially. Additionally, if we overestimate usage, we may incur additional expenses in adding infrastructure, without a commensurate increase in revenues, which would harm our gross margins and other operating results.

The market for advertising cloud solutions is relatively new and dependent on growth in various digital advertising channels. If this market develops more slowly or differently than we expect, our business, growth prospects and financial condition would be adversely affected.

The market for advertising cloud solutions such as ours is relatively new and these solutions may not achieve or sustain high levels of demand and market acceptance. While search and display advertising has been used successfully for several years, marketing via new cloud-based advertising channels such as mobile and social media is not as well established. The future growth of our business could be constrained by the level of acceptance and expansion of emerging cloud-based advertising channels, as well as the continued use and growth of existing channels, such as search and display advertising. Even if these channels become widely adopted, advertisers and agencies may not make significant investments in solutions such as ours that help them manage their digital advertising spend across publisher platforms and advertising channels. It is difficult to predict customer adoption rates, customer demand for our platform, the future growth rate and size of the advertising cloud solutions market or the entry of competitive solutions. Any expansion of the market for advertising cloud solutions depends on a number of factors, including the growth of the cloud-based advertising market, the growth of social and mobile as advertising channels and the cost, performance and perceived value associated with advertising cloud solutions. If advertising cloud solutions do not achieve widespread adoption, or there is a reduction in demand for digital advertising caused by weakening economic conditions, decreases in corporate spending or otherwise, it could result in reduced usage, which could decrease revenues or otherwise adversely affect our business.

If we are unable to maintain our relationships with, and access to, publishers, advertising exchange platforms and other platforms that aggregate the supply of advertising inventory, our business will suffer.

We currently depend on relationships with various publishers, including Baidu, Bing, Facebook, Google, Twitter, Yandex, Yahoo! and Yahoo! Japan, as well as advertising exchange platforms and aggregators of advertising inventory, including Google s DoubleClick Ad Exchange, Yahoo! s Right Media, Facebook s Exchange, Microsoft s Ad Exchange, Twitter s MoPub and AppNexus. Our subscription services interface with these publishers platforms through APIs, such as the Google AdWords API or Facebook API. We are subject to the respective platforms standard API terms and conditions, which govern the use and distribution of data from these platforms. Our business significantly depends on having access to these APIs, particularly the Google AdWords API, which the substantial majority of our customers use, on commercially reasonable terms and our business would be harmed if any of these publishers, advertising exchanges or aggregators of advertising inventory discontinues or limits access to their platforms, modifies their terms of use or other policies or place additional restrictions on us as API users, or charges API license fees for API access. Moreover, some of these publishers, such as Google, market competitive solutions for their platforms. Because the advertising inventory suppliers control their APIs, they may develop competitive offerings that are not subject to the limits imposed on us through the API terms and conditions. Currently, restrictions in these API agreements limit our ability to implement certain functionality, require us to implement functionality in a particular manner or require us to implement certain required minimum functionality, causing us to devote development resources to implement certain functionality that we would not otherwise include in our subscription services and to incur costs for personnel to provide services to implement functionality that we are prohibited from automating. Publishers, advertising exchanges and advertising inventory aggregators update their API terms of use from time to time and new versions of these terms could impose additional restrictions on us. In addition, publishers, advertising

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exchanges and advertising inventory aggregators continually update their APIs and may update or modify functionality, which requires us to modify our software to accommodate these changes and to devote technical resources and personnel to these efforts which could otherwise be used to focus on other priorities. Any of these outcomes could cause demand for our products to decrease, our research and development costs to increase, and our results of operations and financial condition to be harmed.

Our growth depends in part on the success of our relationships with advertising agencies.

Our future growth will depend, in part, on our ability to enter into successful relationships with advertising agencies. Identifying agencies and negotiating and documenting relationships with them requires significant time and resources. These relationships may not result in additional customers or enable us to generate significant revenues. Our contracts for these relationships are typically non-exclusive and do not prohibit the agency from working with our competitors or from offering competing services. Frequently, these agencies do in fact work with our competitors and compete with us. In addition, we often work with, or seek to work with, high-profile brands directly. This may not be possible where, for example, those brands obtain advertising services exclusively or primarily from advertising agencies.

We generally bill agencies for their customers use of our platforms, but in most cases the agency s customer has no direct contractual commitment to make payment to us. Furthermore, some of these agency contracts include provisions whereby the agency is not liable for making payment to us for our subscription services if the agency does not receive a corresponding payment from its client on whose behalf the subscription services were rendered. These provisions may result in longer collections periods or our inability to collect payment for some of our subscription services. If we are unsuccessful in establishing or maintaining our relationships with these agencies on commercially reasonable terms, or if these relationships are not profitable for us, our ability to compete in the marketplace or to grow our revenues could be impaired and our operating results would suffer.

We may not be able to compete successfully against current and future competitors.

The overall market for advertising cloud solutions is rapidly evolving, highly competitive, complex, fragmented, and subject to changing technology and shifting customer needs. We face significant competition in this market and we expect competition to intensify in the future. We currently compete with large, well-established companies, such as Adobe Systems Incorporated and Google Inc. (through its wholly-owned subsidiary DoubleClick), and privately-held companies, such as Kenshoo Ltd. We also compete with channel-specific offerings, in-house proprietary tools, tools from publishers and custom solutions, including spreadsheets. Increased competition may result in reduced pricing for our solutions, longer sales cycles or a decrease of our market share, any of which could negatively affect our revenues and future operating results and our ability to grow our business.

A number of competitive factors could cause us to lose potential sales or to sell our solutions at lower prices or at reduced margins, including, among others:

- potential customers may choose to develop or continue to use internal solutions rather than paying for our solutions or may choose to use a competitor s solution that has different or additional technical capabilities;

- companies may enter our market by expanding their platforms or acquiring a competitor;

some of our competitors, such as Adobe and Google, have greater financial, marketing and technical resources than we do, allowing them to leverage a larger installed customer base, adopt more aggressive pricing policies, and devote greater resources to the development, promotion and sale of their products and services than we can;

companies marketing search, social, display, mobile or web analytics services could bundle advertising cloud solutions or offer such products at a lower price as part of a larger product sale;

channel-specific competitors, such as AdRoll Inc, Criteo S.A., MediaMath Inc., Nanigans, Inc., Rocket Fuel Inc. and Salesforce.com (through its wholly-owned subsidiary Social.com), may devote greater resources to the development, promotion and sale of their channel-specific products and services than we can; and

publishers generally offer their tools for free, or at a reduced price, as their primary compensation is via the sale of advertising on their own or syndicated websites.

We cannot assure you that we will be able to compete successfully against current and future competitors. If we cannot compete successfully, our business, results of operations and financial condition could be negatively impacted.

Our business depends on our customers continued willingness to manage advertising spend on our platforms.

In order for us to improve our operating results, it is important that our customers continue to manage their advertising spend on our platforms, increase their usage and also purchase additional solutions from us. In the case of our direct advertiser customers, we offer our solutions primarily through subscription contracts and generally bill customers over the related subscription period, which is generally one year or longer. During the term of their contracts, our direct advertiser customers generally have no obligation to maintain or increase their advertising spend on our platform beyond a specified minimum monthly fee, which is typically set at the time the contract is signed and is generally greater than half of the monthly amount we anticipate the customer will spend. Our direct advertiser customers generally have no renewal obligation after the initial or then-current renewal subscription period expires, and even if customers renew contracts, they may decrease the level of their digital advertising spend managed through our platform, resulting in lower revenues from that customer. Advertisers that we serve through our arrangements with our advertising agencies generally do not have any contractual commitment to use our platform. Our customers usage may decline or fluctuate as a result of a number of factors, including, but not limited to, their satisfaction with our platforms and our customer support, the frequency and severity of outages, the pricing of our, or competing, solutions, the effects of global economic conditions and reductions in spending levels or changes in our customers strategies regarding digital advertising. Due to our limited historical experience, we may not be able to accurately predict future usage trends. If our customers renew on less favorable terms or reduce their advertising spend on our platforms, our revenues may grow more slowly than expected or decline.

We incur upfront costs associated with onboarding advertisers to our platform and may not recoup our investment if we do not maintain the advertiser relationship over time.

Our operating results may be negatively affected if we are unable to recoup our upfront costs for onboarding new advertisers to our platform. Upfront costs when adding new advertisers generally include sales commissions for our sales force, expenses associated with entering customer data into our platform and other implementation-related costs. Because our customers, including direct advertisers and agencies, are billed over the term of the contract, if new customers sign contracts with short initial subscription periods and do not renew their subscriptions, or otherwise do not continue to use our platform to a level that generates revenues in excess of our upfront expenses, our operating results could be negatively impacted. In cases in which the implementation process is particularly complex, the revenues resulting from the customer under our contract may not cover the upfront investment, so if a significant number of these customers do not renew their contracts, it could negatively affect our operating results.

Because we generally bill our customers over the term of the contract, near term decline in new or renewed subscriptions may not be reflected immediately in our operating results.

Most of our revenues in each quarter are derived from contracts entered into with our customers during previous quarters. Consequently, a decline in new or renewed subscriptions in any one quarter may not be fully reflected in our revenues for that quarter. Such declines, however, would negatively affect our revenues in future periods and the effect of significant downturns in sales and market acceptance of our solutions, and potential changes in our rate of renewals or renewal terms, may not be fully reflected in our results of operations until future periods. In addition, we may be unable to adjust our cost structure rapidly, or at all, to take account of reduced revenues. Our subscription model also makes it difficult for us to rapidly increase our total revenues through additional sales in any period, as revenues from new customers must be earned over the applicable subscription term based on the value of their monthly advertising spend.

We have been dependent on our customers use of search advertising. Any decrease in the use of search advertising or our inability to further penetrate social and display advertising channels would harm our business, growth prospects, operating results and financial condition.

Historically, our customers have primarily used our solutions for managing their search advertising, including mobile search advertising, and the substantial majority of our revenues are derived from advertisers that use our platform to manage their search advertising. We expect that search advertising will continue to be the primary channel used by our customers for the foreseeable future. Should our customers lose confidence in the value or effectiveness of search advertising, the demand for our solutions may decline. In addition, our failure to achieve market acceptance of our solution for the management of social and display advertising spend would harm our growth prospects, operating results and financial condition.

Our sales cycle can be long and unpredictable and require considerable time and expense, which may cause our operating results to fluctuate.

The sales cycle for our solutions, from initial contact with a potential lead to contract execution and implementation, varies widely by customer, but is typically one to nine months. Some of our customers undertake a significant evaluation process that frequently involves not only our solutions but also those of our competitors, which has in the past resulted in extended sales cycles. Our sales efforts involve educating our customers about the use, technical capabilities and benefits of our platform. In addition, under certain circumstances, we sometimes offer an initial term, typically of a few months in duration, to new customers who may terminate their subscription at any time during this initial period before the fixed term contract commences. We have no assurance that the substantial time and money spent on our sales efforts will produce any sales. If our sales efforts result in a new customer subscription, the customer may terminate its subscription during the initial period, after we have incurred the expenses associated with entering the customer s data in our platform and related training and support. If sales expected from a customer are not realized in the time period expected or not realized at all, or if a customer terminates during the initial period, our business, operating results and financial condition could be adversely affected.

Our ability to generate revenue depends on our collection of significant amounts of data from various sources.

Our ability to optimize the delivery of internet advertisements for our customers depends on our ability to successfully leverage data, including data that we collect from our customers as well as data provided by publishers and from third parties. Using cookies and similar tracking technologies, we collect information about the interaction of users with our advertisers and publishers websites. Our ability to successfully leverage such data is dependent upon our continued ability to access and utilize such data. Our ability to access and use such data could be restricted by a number of factors, including consumer choice, restrictions imposed by advertisers and publishers, changes in technology, and new developments in laws, regulations, and industry standards.

If consumer resistance to the collection and sharing of the data used to deliver targeted advertising, increased visibility of consent / Do Not Track mechanisms as a result of industry regulatory and/or legal developments, and/or the development and deployment of new technologies result in a material impact on our ability to collect data, this will materially impair the results of our operations.

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Material defects or errors in our software platform could harm our reputation, result in significant costs to us and impair our ability to sell our subscription services.

The software applications underlying our subscription services are inherently complex and may contain material defects or errors, which may cause disruptions in availability, misallocation of advertising spend or other performance problems. Any such errors, defects, disruptions in service or other performance problems with our software platform could negatively impact our customers businesses or the success of their advertising campaigns and cause harm to our reputation. If we have any errors, defects, disruptions in service or other performance problems with our software platform, customers could elect not to renew or reduce their usage or delay or withhold payment to us, which could result in an increase in our provision for doubtful accounts or an increase in the length of collection cycles for accounts receivable. Errors, defects, disruptions in service or other performance problems could also result in customers making warranty or other claims against us, our giving credits to our customers toward future advertising spend or costly litigation. As a result, material defects or errors in our platform could have a material adverse impact on our business and financial performance.

The costs incurred in correcting any material defects or errors in our software platform may be substantial and could adversely affect our operating results. After the release of new versions of our software, defects or errors may be identified from time to time by our internal team and by our customers. We implement bug fixes and upgrades as part of our regularly scheduled system maintenance. If we do not complete this maintenance according to schedule or if customers are otherwise dissatisfied with the frequency and/or duration of our maintenance services, customers could elect not to renew, or delay or withhold payment to us, or cause us to issue credits, make refunds or pay penalties.

We primarily derive our revenues from a single software platform and any factor adversely affecting subscriptions to our platform could harm our business and operating results.

We primarily derive our revenues from sales of a single software platform. As such, any factor adversely affecting subscriptions to our platform, including product release cycles, market acceptance, product competition, performance and reliability, reputation, price competition, and economic and market conditions, could harm our business and operating results.

If mobile connected devices, their operating systems or content distribution channels, including those controlled by our competitors, develop in ways that prevent our advertising campaigns from being delivered to their users, our ability to grow our business will be impaired.

Our success in the mobile channel depends upon the ability of our technology platform to integrate with mobile inventory suppliers and provide advertising for most mobile connected devices, as well as the major operating systems that run on them and the applications that are downloaded onto them. The design of mobile devices and operating systems is controlled by third parties with whom we do not have any formal relationships. These parties frequently introduce new devices, and from time to time they may introduce new operating systems or modify existing ones. Network carriers may also impact the ability to access specified content on mobile devices. If our solution were unable to work on these devices or operating systems, either because of technological constraints or because an operating system or app developer, device maker or carrier wished to impair our ability to purchase inventory and provide advertisements, our ability to generate revenue could be significantly harmed.

We primarily use a single third-party data center to deliver our services. Any disruption of service at this facility could harm our business.

While we utilize two third-party data centers in total, we manage a significant portion of our services and serve substantially all of our customers from only a single third-party data center facility. While we control the actual computer, network and storage systems upon which our platform runs, and deploy them to the data center facility, we do not control the operation of the facility. The owner of the facility has no obligation to renew the agreement with us on commercially reasonable terms, or at all. If we are unable to renew the agreement on commercially reasonable terms, we may be required to transfer to a new facility or facilities, and we may incur significant costs and possible service interruption in connection with doing so.

The facility is vulnerable to damage or service interruption resulting from human error, intentional bad acts, earthquakes, hurricanes, floods, fires, war, terrorist attacks, power losses, hardware failures, systems failures, telecommunications failures and similar events. Moreover, while we have a disaster recovery plan in place, we do not maintain a hot failover instance of our software platform permitting us to immediately switch over in the event of damage or service interruption at our data center. The occurrence of a natural disaster or an act of terrorism, any outages or vandalism or other misconduct, or a decision to close the facility without adequate notice or other unanticipated problems could result in lengthy interruptions in our services.

Any changes in service levels at the facility or any errors, defects, disruptions or other performance problems at or related to the facility that affect our services could harm our reputation and may damage our customers businesses. Interruptions in our services might reduce our revenues, subject us to potential liability, or result in reduced usage of our platform. In addition, some of our customer contracts require us to issue credits for downtime in excess of certain levels and in some instances give our customers the ability to terminate their subscriptions.

We also depend on third-party Internet-hosting providers and continuous and uninterrupted access to the Internet through third-party bandwidth providers to operate our business. If we lose the services of one or more of our Internet-hosting or bandwidth providers for any reason or if their services are disrupted, for example due to viruses or denial-of-service or other attacks on their systems, or due to human error, intentional bad acts, power loss, hardware failures, telecommunications failures, fires, wars, terrorist attacks, floods, earthquakes, hurricanes, tornadoes or similar events, we could experience disruption in our ability to offer our solutions or we could be required to retain the services of replacement providers, which could increase our operating costs and harm our business and reputation.

If we cannot efficiently implement our solutions for customers, we may lose customers.

Our customers have a variety of different data formats, enterprise applications and infrastructure and our platform must support our customers data formats and integrate with complex enterprise applications and infrastructures. If our platform does not currently support a customer s required data format or appropriately integrate with a customer s applications and infrastructure, then we may choose to configure our platform to do so, which would increase our expenses. Additionally, we do not control our customers implementation schedules. As a result, as we have experienced in the past, if our customers do not allocate internal resources necessary to meet their implementation responsibilities or if we face unanticipated implementation difficulties, the implementation may be delayed. Further, in the past, our implementation capacity has at times constrained our ability to successfully implement our solutions for our customers in a timely manner, particularly during periods of high demand. If the customer implementation process is not executed successfully or if execution is delayed, we could incur significant costs, customers could become dissatisfied and decide not to increase usage of our platform, not to use our platform beyond an initial period prior to their term commitment and revenue recognition could be delayed. In addition, competitors with more efficient operating models with lower implementation costs could penetrate our customer relationships.

Additionally, large customers may request or require specific features or functions unique to their particular business processes, which increase our upfront investment in sales and deployment efforts and the revenues resulting from the customers under our typical contract length may not cover the upfront investments. If prospective large customers require specific features or functions that we do not offer, then the market for our solution will be more limited and our business could suffer. In addition, supporting large customers could require us to devote significant development services and support personnel and strain our personnel resources and infrastructure. If we are unable to address the needs of these customers in a timely fashion or further develop and enhance our solution, these customers may not renew their subscriptions, seek to terminate their relationship with us, renew on less favorable terms, or reduce their advertising spend on our platform. If any of these were to occur, our revenues may decline and our operating results could be adversely affected.

If we are unable to maintain or expand our sales and marketing capabilities, we may not be able to generate anticipated revenues.

Increasing our customer base and achieving broader market acceptance of our software platform will depend to a significant extent on our ability to expand our sales and marketing operations and activities. We expect to be substantially dependent on our sales force to obtain new customers. We are expanding our sales team in order to increase revenues from new and existing customers and to further penetrate our existing markets and expand into new markets, but may not be able to attract and hire qualified sales personnel quickly enough or at all. Our solutions require a sophisticated sales force with specific sales skills and technical knowledge. Competition for qualified sales personnel is intense, and we may not be able to retain our existing sales personnel or attract, integrate or retain sufficient highly qualified sales personnel.

Our ability to achieve revenue growth in the future will depend, in large part, on our success in recruiting, training and retaining sufficient numbers of sales personnel. These new employees require significant training and experience before they achieve full productivity. As a result, the cost of hiring and carrying new representatives cannot be offset by the revenues they produce for a significant period of time. Our recent hires and planned hires may not become productive as quickly as we would like, and we may not be able to hire or retain sufficient numbers of qualified individuals in the markets where we do business. Our business will be seriously harmed if these expansion efforts do not work as planned or generate a corresponding significant increase in revenues.

Any failure to offer high-quality technical support services may adversely affect our relationships with our customers and harm our financial results.

Our customers depend on our support organization to resolve any technical issues relating to our solutions. In addition, our sales process is highly dependent on the quality of our solutions, our business reputation and on strong recommendations from our existing customers. Any failure to maintain high-quality technical support, or a market perception that we do not maintain high-quality support, could harm our reputation, adversely affect our ability to sell our solutions to existing and prospective customers, and harm our business, operating results and financial condition.

We offer technical support services with our solutions and may be unable to respond quickly enough to accommodate short-term increases in customer demand for support services. We also may be unable to modify the format of our support services to compete with changes in support services provided by competitors. It is difficult to predict customer demand for technical support services and if customer demand increases significantly, we may be unable to provide satisfactory support services to our customers. Additionally, increased customer demand for these services, without corresponding revenues, could increase costs and adversely affect our operating results.

If our security measures are breached or unauthorized access to customer data or our data is otherwise obtained, our solutions may be perceived as not being secure, customers may reduce the use of or stop using our solutions and we may incur significant liabilities.

In the ordinary course of our business, we maintain sensitive data on our networks, including our intellectual property and proprietary or confidential business information relating to our business and that of our customers and business partners. The secure maintenance of this information is critical to our business and reputation. We believe that companies have been increasingly subject to a wide variety of security incidents, cyber-attacks and other attempts to gain unauthorized access. These threats can come from a variety of sources, ranging in sophistication from an individual hacker to a state-sponsored attack. Cyber threats may be generic, or they may be custom-crafted against our information systems. Over the past year, cyber-attacks have become more prevalent and much harder to detect and defend against. Our network and storage applications may be subject to unauthorized access by hackers or breached due to operator error, malfeasance or other system disruptions. It is often difficult to anticipate or immediately detect such incidents and the damage caused by such incidents. These data breaches and any unauthorized access or disclosure of our information or intellectual property could result in the loss of information, litigation, indemnity obligations and other liability. While we have security measures in place, our systems and networks are subject to ongoing threats and therefore these security measures may be breached as a result of third-party action, including cyber-attacks or other intentional misconduct by computer hackers, employee error, malfeasance or otherwise. This could result in one or more third parties obtaining unauthorized access to our customers data or our data, including intellectual property and other confidential business information. Because techniques used to obtain unauthorized access or to sabotage systems change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. Third parties may also attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information in order to gain access to our customers data or our data, including intellectual property and other confidential business information. If an actual or perceived breach of our security occurs, the market perception of the effectiveness of our security measures could be harmed, we could lose potential sales and existing customers or we could incur other liabilities, which could adversely affect our business.

We must develop and introduce enhancements and new features that achieve market acceptance or that keep pace with technological developments to remain competitive in our evolving industry.

We operate in a dynamic market characterized by rapidly changing technologies and industry and legal standards. The introduction of new advertising cloud solutions by our competitors, the market acceptance of solutions based on new or alternative technologies, or the emergence of new industry standards could render our platform obsolete. Our ability to compete successfully, attract new customers and increase revenues from existing customers depends in large part on our ability to enhance and improve our existing cross-channel performance advertising cloud platform and to continually introduce or acquire new features that are in demand by the market we serve. We also must update our software to reflect changes in publishers APIs and terms of use. The success of any enhancement or new solution depends on several factors, including timely completion, adequate quality testing, appropriate introduction and market acceptance. Any new platform or feature that we develop or acquire may not be introduced in a timely or cost-effective manner, may contain defects or may not achieve the broad market acceptance necessary to generate significant revenues. If we are unable to anticipate or timely and successfully develop or acquire new offerings or features or enhance our existing platform to meet customer requirements, our business and operating results will be adversely affected.

Our growth depends in part on the success of our strategic relationships with third parties.

Our future growth will depend on our ability to enter into successful strategic relationships with third parties. For example, we are seeking to establish relationships with third parties to develop integrations with complementary technology and content. These relationships may not result in additional customers or enable us to generate significant revenues. Identifying partners and negotiating and documenting relationships with them require significant time and resources. Our contracts for these relationships are typically non-exclusive and do not prohibit the other party from working with our competitors or from offering competing services. If we are unsuccessful in establishing or maintaining our relationships with these third parties, our ability to compete in the marketplace or to grow our revenues could be impaired and our operating results would suffer.

As a result of our customers increased usage of our software platform, we will need to continually improve our hosting infrastructure to avoid service interruptions or slower system performance.

We have experienced continued growth in the number of advertisers, transactions and data that our hosting infrastructure supports. We seek to maintain sufficient excess capacity in our infrastructure to meet the needs of all of our customers. We also seek to maintain excess capacity to facilitate the rapid provision of new customer deployments and the expansion of existing customer deployments. For example, if we secure a large customer or a group of customers that require significant amounts of bandwidth or storage, we may need to increase bandwidth, storage, power or other elements of our application architecture and our infrastructure, and our existing systems may not be able to scale in a manner satisfactory to our existing or prospective customers.

The amount of infrastructure needed to support our customers is based on our estimates of anticipated usage. If we were to experience unforeseen increases in usage, we could be required to increase our infrastructure investments resulting in increased costs or reduced gross margins, and if we do not accurately predict our infrastructure capacity requirements, our customers could experience service outages that may subject us to financial penalties and liabilities and result in customer losses. If our hosting infrastructure capacity fails to keep pace with increased sales, customers may experience service interruptions or slower system performance as we seek to obtain additional capacity, which could harm our reputation and adversely affect our revenue growth. As use of our software platform grows and as customers use it for more complicated tasks, we will need to devote additional resources to improving our application architecture and our infrastructure in order to maintain the performance of our software platform. We may need to incur additional costs to upgrade or expand our computer systems and architecture in order to accommodate increased demand if our systems cannot handle current or higher volumes of usage. In addition, increasing our systems and infrastructure in advance of new customers would cause us to have increased cost of revenues, which can adversely affect our gross margins until we increase revenues that are spread over the increased costs.

Any failure to protect our intellectual property rights could impair our ability to protect our proprietary technology and our brand.

Our success and ability to compete depends in part upon our intellectual property. We primarily rely on a combination of copyright, trade secret and trademark laws, as well as confidentiality procedures and contractual restrictions with our employees, customers, partners and others to establish and protect our intellectual property rights. However, the steps we take to protect our intellectual property rights may be inadequate or we may be unable to secure intellectual property protection for all of our solutions. In particular, we have two issued U.S. patents.

If we are unable to protect our intellectual property, our competitors could use our intellectual property to market products and services similar to ours and our ability to compete effectively would be impaired. Moreover, others may independently develop technologies that are competitive to ours or infringe our intellectual property. The enforcement of our intellectual property rights depends on our legal actions against these infringers being successful, but we cannot be sure these actions will be successful, even when our rights have been infringed. In addition, defending our intellectual property rights might entail significant expense and diversion of management resources. Any of our intellectual property rights may be challenged by others or invalidated through administrative processes or litigation. Any patents issued in the future may not provide us with competitive advantages or may be successfully challenged by third parties.

Furthermore, legal standards relating to the validity, enforceability and scope of protection of intellectual property rights are uncertain. Effective protection of our intellectual property may not be available to us in every country in which our solutions are available. The laws of some foreign countries may not be as protective of intellectual property rights as those in the United States, and mechanisms for enforcement of intellectual property rights may be inadequate. Accordingly, despite our efforts, we may be unable to prevent third parties from infringing upon or misappropriating our intellectual property.

We might be required to spend significant resources to monitor and protect our intellectual property rights, and our efforts to enforce our intellectual property rights may be met with defenses, counterclaims and countersuits attacking the validity and enforceability of our intellectual property rights. Litigation to protect and

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enforce our intellectual property rights could be costly, time-consuming and distracting to management, whether or not it is resolved in our favor, and could ultimately result in the impairment or loss of portions of our intellectual property.

We could incur substantial costs as a result of any claim of infringement of another party s intellectual property rights.

In recent years, there has been significant litigation in the United States involving patents and other intellectual property rights. Companies in the Internet and technology industries are increasingly bringing and becoming subject to suits alleging infringement of proprietary rights, particularly patent rights, and our competitors may hold patents or have pending patent applications, which could be related to our business. These risks have been amplified by the increase in third parties, which we refer to as non-practicing entities, whose sole primary business is to assert such claims. We have received in the past, and expect to receive in the future, notices that claim we or our customers using our solutions have misappropriated or misused other parties intellectual property rights. If we are sued by a third party that claims that our technology infringes its rights, the litigation could be expensive and could divert our management resources. We do not currently have an extensive patent portfolio of our own, which may limit the defenses available to us in any such litigation.

In addition, in most instances, we have agreed to indemnify our customers against certain claims that our subscription services infringe the intellectual property rights of third parties. Our business could be adversely affected by any significant disputes between us and our customers as to the applicability or scope of our indemnification obligations to them. The results of any intellectual property litigation to which we might become a party, or for which we are required to provide indemnification, may require us to do one or more of the following:

- cease offering or using technologies that incorporate the challenged intellectual property;
- make substantial payments for legal fees, settlement payments or other costs or damages;
- obtain a license, which may not be available on reasonable terms, to sell or use the relevant technology; or
- redesign technology to avoid infringement.

If we are required to make substantial payments or undertake any of the other actions noted above as a result of any intellectual property infringement claims against us or any obligation to indemnify our customers for such claims, such payments or costs could have a material adverse effect upon our business and financial results.

Our use of open source technology could impose limitations on our ability to commercialize our software platform.

We use open source software in our platform. Some open source software licenses require users who distribute open source software as part of their software to publicly disclose all or part of the source code to such software and/or make available any derivative works of the open source code on unfavorable terms or at no cost. The terms of various open source licenses have not been interpreted by the U.S. courts, and there is a risk that such licenses could be construed in a manner that imposes unanticipated conditions or restrictions on our ability to market our software platform. While we monitor our use of open source software and try to ensure that none is used in a manner that would require us to disclose our source code or that would otherwise breach the terms of an open source agreement, such use could inadvertently occur and we may be required to release our proprietary source code, pay damages for breach of contract, re-engineer our applications, discontinue sales in the event re-engineering cannot be accomplished on a timely basis or take other remedial action that may divert resources away from our development efforts, any of which could cause us to breach customer contracts, harm our reputation, result in customer losses or claims, increase our costs or otherwise adversely affect our business and operating results.

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If the market for cloud-based software develops more slowly than we expect or declines, our business could be harmed.

The cloud computing market is not as mature as the market for on-premise software, and it is uncertain whether cloud computing will achieve and sustain high levels of customer demand and market acceptance. If other cloud computing providers experience security incidents, loss of customer data, disruptions in delivery or other problems, the market for cloud computing as a whole, including our solution, may be negatively affected. If cloud computing does not achieve widespread adoption, or there is a reduction in demand for cloud computing caused by a lack of customer acceptance, technological challenges, weakening economic conditions, security or privacy concerns, competing technologies and products, decreases in corporate spending or otherwise, it could result in decreased revenues or increased expenses from development of alternative on-premise solutions and our business could be adversely affected.

Because our long-term success depends, in part, on our ability to expand our sales to customers outside the United States, our business will be susceptible to risks associated with international operations.

We currently maintain offices and/or have sales personnel in Australia, China, England, France, Germany, Ireland, Japan and Singapore, as well as the United States. As we continue to expand our customer base outside the United States, our business will be increasingly susceptible to risks associated with international operations. However, we have a limited operating history outside the United States, and our ability to manage our business and conduct our operations internationally requires considerable management attention and resources and is subject to particular challenges of supporting a rapidly growing business in an environment of diverse cultures, languages, customs, tax laws, legal systems, alternate dispute systems and regulatory systems. The risks and challenges associated with international expansion include:

- the need to support and integrate with local publishers and partners;
- continued localization of our platform, including translation into foreign languages and associated expenses;
- competition with companies that have greater experience in the local markets than we do or who have pre-existing relationships with potential customers in those markets;
- compliance with multiple, potentially conflicting and changing governmental laws and regulations, including employment, tax, privacy and data protection laws and regulations;
- compliance with anti-bribery laws, including compliance with the Foreign Corrupt Practices Act;
- difficulties in invoicing and collecting in foreign currencies and associated foreign currency exposure;

- difficulties in staffing and managing foreign operations and the increased travel, infrastructure and legal compliance costs associated with international operations;

- different or lesser protection of our intellectual property rights;

- difficulties in enforcing contracts and collecting accounts receivable, longer payment cycles and other collection difficulties;

- restrictions on repatriation of earnings; and

- regional economic and political conditions.

We have limited experience in marketing, selling and supporting our subscription services internationally, which increases the risk that any potential future expansion efforts that we may undertake will not be successful.

Fluctuations in the exchange rate of foreign currencies could result in currency transactions losses.

We currently have foreign sales denominated in Australian dollars, British pound sterling, Canadian dollars, Chinese yuan, euros, Japanese yen and Singapore dollars. In addition, we incur a portion of our operating expenses in the currencies of the countries where we have offices. We face exposure to adverse movements in currency exchange rates, which may cause our revenues and operating results to differ materially from expectations. If the U.S. dollar strengthens relative to foreign currencies, our non-U.S. revenues would be adversely affected. Conversely, a decline in the U.S. dollar relative to foreign currencies would increase our non-U.S. revenues when translated into U.S. dollars. Our operating results could be negatively impacted depending on the amount of expense denominated in foreign currencies. As exchange rates vary, revenues, cost of revenues, operating expenses and other operating results, when translated, may differ materially from expectations. In addition, our revenues and operating results are subject to fluctuation if our mix of U.S. and foreign currency denominated transactions or expenses changes in the future because we do not currently hedge our foreign currency exposure. Even if we were to implement hedging strategies to mitigate foreign currency risk, these strategies might not eliminate our exposure to foreign exchange rate fluctuations and would involve costs and risks of their own, such as ongoing management time and expertise, external costs to implement the strategies and potential accounting implications.

If we fail to develop widespread brand awareness cost-effectively, our business may suffer.

We believe that developing and maintaining widespread awareness of our brand in a cost-effective manner is critical to achieving widespread acceptance of our solution and attracting new customers. We expect sales and marketing expenses to increase as a result of our marketing and brand promotion activities. We may not generate customer awareness or increase revenues enough to offset the increased expenses we incur in building our brand. If we fail to successfully promote and maintain our brand, or incur substantial marketing and sales expenses, which are not offset by increased revenues, we may fail to attract or retain customers necessary to realize a sufficient return on our brand-building efforts, or to achieve the widespread brand awareness that is essential for broad customer adoption of our solution.

Unfavorable conditions in the market for digital advertising or the global economy or reductions in digital advertising spend could limit our ability to grow our business and negatively affect our operating results.

Revenue growth and potential profitability of our business depends on digital advertising spend by advertisers in the markets we serve. Our operating results may vary based on changes in the market for digital advertising or the global economy. To the extent that weak economic conditions cause our customers and potential customers to freeze or reduce their advertising budgets, particularly digital advertising, demand for our solution may be negatively affected.

Historically, economic downturns have resulted in overall reductions in advertising spend. If economic conditions deteriorate or the rise of geopolitical instability and military hostilities causes economic uncertainty, our customers and potential customers may elect to decrease their advertising budgets or defer or reconsider software and service purchases, which would limit our ability to grow our business and negatively affect our operating results.

Our business depends on retaining and attracting qualified personnel, and turnover may result in operational inefficiencies that could negatively affect our business.

Our success depends upon the continued service of our talented management, operational and key technical employees, as well as our ability to continue to attract additional highly qualified talent. Turnover amongst our employees could result in operational and administrative inefficiencies and added costs, which could adversely impact our results of operations, stock price and customer relationships. In addition, we must successfully integrate any new personnel that we hire within our organization in order to achieve our operating objectives, and changes in other key positions may temporarily affect our financial performance and results of operations as new employees become familiar with our business.

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We do not maintain key person life insurance policies on any of our employees. Each of our executive officers, key technical personnel and other employees could terminate his or her relationship with us at any time. Our business also requires skilled technical, sales and other personnel, who are in high demand and are often subject to competing offers. As we expand into additional geographic markets, we will require personnel with expertise in these new areas. Competition for qualified employees is intense in our industry and particularly in San Francisco, California, where most of our employees are based. An inability to retain, attract, relocate and motivate employees required for our business, including the planned expansion of our business, could delay or prevent the achievement of our business objectives and could materially harm our business and our customer relationships.

Our business and operations have experienced rapid growth in recent periods, which has placed, and may continue to place, significant demands on our management and infrastructure. If we fail to manage our growth effectively, we may be unable to execute our business plan, maintain high levels of service or address competitive challenges adequately.

We increased our number of full-time employees from 285 as of December 31, 2011 to 571 as of December 31, 2014. Our growth has placed, and may continue to place, a significant strain on our managerial, administrative, operational, financial and other resources. We intend to further expand our overall headcount and operations both domestically and internationally, with no assurance that we will be able to meet our hiring plans or that our business or revenues will continue to grow. Creating a global organization and managing a geographically dispersed workforce will require substantial management effort, the allocation of valuable management resources and significant additional investment in our infrastructure. We will be required to continue to improve our operational, financial and management controls and our reporting procedures and we may not be able to do so effectively. Further, to accommodate our expected growth we must continually improve and maintain our technology, systems and network infrastructure. As such, we may be unable to manage our expenses effectively in the future, which may negatively impact our gross margins or operating expenses in any particular quarter. If we fail to manage our anticipated growth or change in a manner that does not preserve the key aspects of our corporate culture, the quality of our solutions may suffer, which could negatively affect our brand and reputation and harm our ability to retain and attract customers.

Domestic and foreign government regulation and enforcement of data practices and data tracking technologies is expansive, not clearly defined and rapidly evolving. Such regulation could directly restrict portions of our business or indirectly affect our business by constraining our customers use of our platform or limiting the growth of our markets.

Federal, state, municipal and/or foreign governments and agencies have adopted and could in the future adopt, modify, apply or enforce laws, policies, and regulations covering user privacy, data security, technologies such as cookies that are used to collect, store and/or process data, the taxation of products and services, unfair and deceptive practices, and/or the collection, use, processing, transfer, storage and/or disclosure of data associated with a unique individual. The categories of data regulated under these laws vary widely and are often ill-defined and subject to new applications or interpretation by regulators. Our subscription services enable our customers to collect, manage and store data regarding the measurement and valuation of their digital advertising and marketing campaigns, which may include data that is directly or indirectly obtained or derived through the activities of online or mobile visitors. The uncertainty and inconsistency among these laws, coupled with a lack of guidance as to how these laws will be applied to current and emerging Internet and mobile analytics technologies, creates a risk that regulators, lawmakers or other third parties, such as potential plaintiffs, may assert claims, pursue investigations or audits, or engage in civil or criminal enforcement. These actions could limit the market for our subscription services or impose burdensome requirements on our services and/or customers use of our services, thereby rendering our business unprofitable.

Some features of our subscription services use cookies, which trigger the data protection requirements of certain foreign jurisdictions, such as the EU Cookie Directive. In addition, although our subscription services do not involve the collection or use of personally identifiable information from visitors, our services collect anonymous data about visitors interactions with our advertiser clients that may be subject to regulation under current or future laws or regulations. If our privacy or data security measures fail to comply with these current or future laws and regulations in any of the jurisdictions in which we collect information, we may be subject to litigation, regulatory investigations, civil or criminal enforcement, audits or other liabilities in such jurisdictions, or our advertisers may terminate their relationships with us.

This area of the law is currently under intense government scrutiny and many governments, including the U.S. government, are considering a variety of proposed regulations that would restrict or impact the conditions under which data obtained from or through the activities of visitors could be collected, processed or stored. In addition, regulators such as the Federal Trade Commission and the California Attorney General are continually proposing new regulations and interpreting and applying existing regulations in new ways. Changes to existing laws or new laws regulating the solicitation, collection or processing of personal and consumer information, truth-in-advertising and consumer protection could affect our customers utilization of digital advertising and marketing, potentially reducing demand for our subscription services, or impose restrictions that make it more difficult or expensive for us to provide our services.

If legislation dampens the growth in web and mobile usage or access to the Internet, our results of operations could be harmed.

Legislation enacted in the future could dampen the growth in web and mobile usage and decrease its acceptance as a medium of communications and commerce or result in increased adoption of new modes of communication and commerce that may not be serviced by our products. In addition, government agencies or private organizations may begin to impose taxes, fees or other charges for accessing the Internet, which could result in slower growth or a decrease in ecommerce, use of social media and/or use of mobile devices. Any of these outcomes could cause demand for our platform to decrease, our costs to increase, and our results of operations and financial condition to be harmed.

If our customers fail to abide by applicable privacy laws or to provide adequate notice and/or obtain consent from end users, we could be subject to litigation or enforcement action or reduced demand for our services. Industry self-regulatory standards may be implemented in the future that could affect demand for our platform and our ability to access data we use to provide our platform.

Our customers utilize our services to support and measure their direct interactions with visitors and we must rely on our customers to implement and administer any notice or choice mechanisms required under applicable laws. If customers fail to abide by these laws, it could result in litigation or regulatory or enforcement action against our customers or against us directly.

In addition, self-regulatory organizations (such as the Network Advertising Initiative) to which our customers may belong may impose opt-in or opt-out requirements on our customers, which may in the future require our customers to provide various mechanisms for users to opt-in or opt-out of the collection of any data, including anonymous data, with respect to such users web or mobile activities. The online and/or mobile industries may adopt technical or industry standards, or federal, state, local or foreign laws may be enacted that allow users to opt-in or opt-out of data that is necessary to our business. In particular, some government regulators and standard-setting organizations have suggested- a Do Not Track standard that allows users to express a preference, independent of cookie settings in their browser, not to have website browsing recorded. All the major internet browsers have implemented some version of a Do Not Track setting. Furthermore, publishers may implement alternative tracking technologies that make it more difficult to access the data necessary to our business or make it more difficult for us to compete with the publisher s own advertising management solutions. If any of these events were to occur in the future, it could have a material effect on our ability to provide services and for our customers to collect the data that is necessary to use our services.

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Our revenues may be adversely affected if we are required to charge sales taxes in additional jurisdictions or other taxes for our solutions.

We collect or have imposed upon us sales or other taxes related to the solutions we sell in certain states and other jurisdictions. Additional states, countries or other jurisdictions may seek to impose sales or other tax collection obligations on us in the future, or states or jurisdictions in which we already pay tax may increase the amount of taxes we are required to pay. A successful assertion by any state, country or other jurisdiction in which we do business that we should be collecting sales or other taxes on the sale of our products and services could, among other things, create significant administrative burdens for us, result in substantial tax liabilities for past sales, discourage clients from purchasing solutions from us or otherwise substantially harm our business and results of operations.

We may experience quarterly fluctuations in our operating results due to a number of factors which make our future results difficult to predict and could cause our operating results to fall below expectations or our guidance.

Our quarterly operating results may fluctuate due to a variety of factors, many of which are outside of our control. As a result, comparing our operating results on a period-to-period basis may not be meaningful. You should not rely on our past results as indicative of our future performance. If our revenues or operating results fall below the expectations of investors or securities analysts, or below any guidance we may provide to the market, the price of our common stock could decline substantially.

In addition to other risk factors listed in this section, factors that may affect our quarterly operating results include the following:

- the level of advertising spend managed through our platform for a particular quarter;
- customer renewal rates, and the pricing and usage of our platform in any renewal term;
- demand for our platform and the size and timing of our sales;
- customers delaying purchasing decisions in anticipation of new releases by us or of new products by our competitors;
- network outages or security breaches and any associated expenses;
- changes in the competitive dynamics of our industry, including consolidation among competitors or customers;
- market acceptance of our current and future solutions;

- changes in spending on digital advertising or information technology and software by our current and/or prospective customers;
- budgeting cycles of our customers;
- our potentially lengthy sales cycle;
- our ability to control costs, including our operating expenses;
- the amount and timing of infrastructure costs and operating expenses related to the maintenance and expansion of our business, operations and infrastructure;
- foreign currency exchange rate fluctuations; and
- general economic and political conditions in our domestic and international markets.

Based upon all of the factors described above, we have a limited ability to forecast our future revenues, costs and expenses, and as a result, our operating results may from time to time fall below our estimates or the expectations of public market analysts and investors.

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We might require additional capital to support business growth, and this capital might not be available on acceptable terms, if at all.

We intend to continue to make investments to support our business growth and may require additional funds to respond to business challenges, including the need to develop new features or enhance our existing platform, improve our operating infrastructure or acquire complementary businesses and technologies. Accordingly, we may need to engage in equity or debt financings to secure additional funds. If we raise additional funds through further issuances of equity or convertible debt securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock. Any debt financing secured by us in the future could involve restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions. In addition, we may not be able to obtain additional financing on terms favorable to us, if at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us, when we require it, our ability to continue to support our business growth and to respond to business challenges could be significantly impaired.

Future acquisitions, strategic investments, partnerships or alliances could be difficult to integrate, divert the attention of key management personnel, disrupt our business, dilute shareholder value and adversely affect our results of operations and financial condition.

We recently acquired NowSpots, Inc., doing business as Perfect Audience (Perfect Audience) in June 2014 and SocialMoov, a Paris-based company, in February 2015 and may seek to acquire additional businesses, products or technologies in the future. However, we have limited experience in acquiring and integrating businesses, products and technologies. If we identify an appropriate acquisition candidate, we may not be successful in negotiating the terms and/or financing of the acquisition, and our due diligence may fail to identify all of the problems, liabilities or other shortcomings or challenges of an acquired business, product or technology, including issues related to intellectual property, product quality or architecture, regulatory compliance practices, revenue recognition or other accounting practices or employee or client issues.

Any acquisition or investment may require us to use significant amounts of cash, issue potentially dilutive equity securities or incur debt. In addition, acquisitions, including our recent acquisitions of Perfect Audience and SocialMoov, involve numerous risks, any of which could harm our business, including:

- regulatory and commercial risks relating to retargeting of online advertising and social advertising, the primary businesses of Perfect Audience and SocialMoov, respectively;
- difficulties in integrating the operations, technologies, services and personnel of acquired businesses, especially if those businesses operate outside of our core competency;
- cultural challenges associated with integrating employees from the acquired company into our organization;
- reputation and perception risks associated with the acquired product or technology by the general public;

ineffectiveness or incompatibility of acquired technologies or services;

potential loss of key employees of acquired businesses;

inability to maintain the key business relationships and the reputations of acquired businesses;

diversion of management s attention from other business concerns;

litigation for activities of the acquired company, including claims from terminated employees, clients, former shareholders or other third parties;

failure to identify all of the problems, liabilities or other shortcomings or challenges of an acquired company, technology, or solution, including issues related to intellectual property, solution quality or

- architecture, regulatory compliance practices, revenue recognition or other accounting practices or employee or client issues;

- in the case of foreign acquisitions such as SocialMoov, the need to integrate operations across different cultures and languages and to address the particular economic, currency, political and regulatory risks associated with specific countries; costs necessary to establish and maintain effective internal controls for acquired businesses;

- failure to successfully further develop the acquired technology in order to recoup our investment; and

- increased fixed costs.

If we are unable to successfully integrate Perfect Audience and SocialMoov, or any future business, product or technology we acquire, our business and results of operations may suffer.

In addition, a significant portion of the purchase price of companies we acquire may be allocated to acquired goodwill and other intangible assets, which must be assessed for impairment at least annually. If our acquisitions do not yield expected returns, we may be required to take charges to our operating results based on this impairment assessment process, which could adversely affect our results of operations.

Acquisitions could also result in dilutive issuances of equity securities or the incurrence of debt, which could adversely affect our operating results. For instance, in connection with our acquisition of Perfect Audience, we issued 1.7 million shares of our common stock, and the SocialMoov acquisition in February 2015 would require us to issue up to 1.6 million shares of our common stock.

If we are unable to implement and maintain effective internal control over financial reporting in the future, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock may be negatively affected.

As a public company, we are required to maintain internal control over financial reporting and to report any material weaknesses in such internal control. Section 404 of the Sarbanes-Oxley Act of 2002 (the Sarbanes-Oxley Act) requires that we evaluate and determine the effectiveness of our internal control over financial reporting and provide a management report on the internal control over financial reporting and a report by our independent registered public accounting firm to the extent we decide not to avail ourselves of the exemption provided to an emerging growth company, as defined by The Jumpstart Our Business Act of 2012. If we have a material weakness in our internal control over financial reporting, we may not detect errors on a timely basis and our financial statements may be materially misstated. In addition, in the future if we identify material weaknesses in our internal control over financial reporting, if we are unable to comply with the requirements of Section 404 in a timely manner, if we are unable to assert that our internal control over financial reporting is effective or if our independent registered public accounting firm is unable to express an opinion as to the effectiveness of our internal control over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock could be negatively affected, and we could become subject to investigations by the stock exchange on which our securities are listed, the SEC, or other regulatory authorities, which could require additional financial and management resources.

We are an emerging growth company, and we cannot be certain if the reduced disclosure requirements applicable to emerging growth companies will make our common stock less attractive to investors.

For as long as we continue to be an emerging growth company, we intend to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies including, but not limited to, the exemption from the requirement of a report on our internal control over financial reporting by our independent registered public accounting firm, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. We cannot predict if investors will find our common stock less attractive because we will rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

We will remain an emerging growth company until the earliest of (i) the end of the fiscal year in which the market value of our common stock that is held by non-affiliates exceeds $700 million as of June 30, (ii) the end of the fiscal year in which we have total annual gross revenues of $1 billion or more during such fiscal year, (iii) the date on which we issue more than $1 billion in non-convertible debt in a three-year period or (iv) March 21, 2018.

We may not be able to utilize a significant portion of our net operating loss or research tax credit carryforwards, which could adversely affect our profitability.

As of December 31, 2014, we had federal and state net operating loss carryforwards due to prior period losses, which if not utilized will begin to expire in 2026 and 2016 for federal and state purposes, respectively. We also have federal research tax credit carryforwards, which if not utilized will begin to expire in 2026. These net operating loss and research tax credit carryforwards could expire unused and be unavailable to offset future income tax liabilities, which could adversely affect our profitability.

In addition, under Section 382 of the Internal Revenue Code of 1986, as amended (the Code), our ability to utilize net operating loss carryforwards or other tax attributes, such as research tax credits, in any taxable year may be limited if we experience an ownership change. A Section 382 ownership change generally occurs if one or more stockholders or groups of stockholders who own at least 5% of our stock increase their ownership by more than 50 percentage points over their lowest ownership percentage within a rolling three-year period. Similar rules may apply under state tax laws.

Future issuances of our stock could cause an ownership change. It is possible that any future ownership change could have a material effect on the use of our net operating loss carryforwards or other tax attributes, which could adversely affect our profitability.

Our reported financial results may be adversely affected by changes in accounting principles generally accepted in the United States.

Generally accepted accounting principles in the United States are subject to interpretation by the Financial Accounting Standards Board (FASB), the SEC, and various bodies formed to promulgate and interpret appropriate accounting principles. A change in these principles or interpretations could have a significant effect on our reported financial results, and could affect the reporting of transactions completed before the announcement of a change.

Risks Related to the Ownership of Our Common Stock

The trading prices of the securities of technology companies have been highly volatile. Accordingly, the market price of our common stock has been, and is likely to continue to be, subject to wide fluctuations and could subject us to litigation.

Factors affecting the market price of our common stock include:

variations in our revenue, billings, gross margin, operating results, free cash flow, loss per share, number of active advertisers, revenue retention rates, annualized advertising spend on our platform, adjusted EBITDA and how these results compare to analyst expectations;

forward looking guidance on billings, revenue, gross margin, operating results, free cash flow, and loss per share;

- announcements of technological innovations, new products or services, strategic alliances, acquisitions or significant agreements by us or by our competitors;
- disruptions in our cloud-based operations or services or disruptions of other prominent cloud-based operations or services;
- the economy as a whole, market conditions in our industry, and the industries of our customers; and
- any other factors discussed herein.

In addition, the stock market in general has experienced substantial price and volume volatility that is often seemingly unrelated to the operating results of any particular companies. Moreover, if the market for technology stocks, especially advertising cloud and cloud computing-related stocks, or the stock market in general experiences uneven investor confidence, the market price of our common stock could decline for reasons unrelated to our business, operating results or financial condition. The market price for our stock might also decline in reaction to events that affect other companies within, or outside, our industry, even if these events do not directly affect us. Some companies that have experienced volatility in the trading price of their stock have been subject of securities litigation. If we are the subject of such litigation, it could result in substantial costs and a diversion of management s attention and resources.

We do not intend to pay dividends for the foreseeable future.

We have never declared nor paid cash dividends on our capital stock. We currently intend to retain any future earnings to finance the operation and expansion of our business, and we do not expect to declare or pay any dividends in the foreseeable future. Consequently, stockholders must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investment.

Our directors, officers and their respective affiliates own a significant percentage of our stock and will be able to exert significant control over matters subject to stockholder approval.

As of December 31, 2014, our directors, officers and their respective affiliates, beneficially owned approximately 21.0% of our outstanding voting stock. Therefore, these stockholders will continue to have the ability to influence us through this ownership position. These stockholders may be able to determine all matters requiring stockholder approval. For example, these stockholders could be able to control elections of directors, amendments of our organizational documents, or approval of any merger, sale of assets, or other major corporate transaction. This may prevent or discourage unsolicited acquisition proposals or offers for our common stock that you may feel are in your best interest as one of our stockholders.

If there are substantial sales of shares of our common stock, the price of our common stock could decline.

Sales of a substantial number of shares of our common stock in the public market, or the perception that these sales might occur could depress the market price of our common stock and may make it more difficult for you to sell your common stock at a time and price that you deem appropriate. We are unable to predict the effect that sales may have on the prevailing market price of our common stock. We have a currently effective Registration Statement on Form S-3 registering for sale approximately 1.7 million shares of our common stock in connection with our acquisition of Perfect Audience. In addition, in connection with our acquisition of SocialMoov, we are required to prepare and file a

Registration Statement on Form S-3 registering up to 1.6 million shares of our common stock for sale (some of which are subject to contractual restrictions for a period of nine months from the closing of the acquisition and some of which will not be issued, if at all, until the one and two year anniversaries of the closing of the acquisition). After our initial public offering (IPO) in March 2013, the holders of an aggregate of 18.8 million shares of our common stock had rights, subject to some conditions, to require us to file registration statements covering their shares or to include their shares in registration statements that we may file for ourselves or our stockholders. To the extent the holders of such shares have not sold the shares otherwise, such holders may continue to have registration rights. Registration of these shares under the

Securities Act would result in the shares becoming freely tradable without restriction under the Securities Act. Any sales of securities by existing stockholders could adversely affect the trading price of our common stock.

Delaware law and provisions in our restated certificate of incorporation and restated bylaws could make a merger, tender offer, or proxy contest difficult, thereby depressing the trading price of our common stock.

Our status as a Delaware corporation and the anti-takeover provisions of the Delaware General Corporation Law may discourage, delay, or prevent a change in control by prohibiting us from engaging in a business combination with an interested stockholder for a period of three years after the person becomes an interested stockholder, even if a change of control would be beneficial to our existing stockholders. In addition, our restated certificate of incorporation and restated bylaws contain provisions that may make the acquisition of our Company more difficult, including the following:

- our board of directors are classified into three classes of directors with staggered three-year terms and directors can only be removed from office for cause;

- only our board of directors has the right to fill a vacancy created by the expansion of our board of directors or the resignation, death or removal of a director, which prevents stockholders from being able to fill vacancies on our board of directors;

- only our chairman of the board, our lead independent director, our chief executive officer, our president, or a majority of our board of directors is authorized to call a special meeting of stockholders;

- certain litigation against us can only be brought in Delaware;

- our restated certificate of incorporation authorizes undesignated preferred stock, the terms of which may be established, and shares of which may be issued, without the approval of the holders of common stock; and

- advance notice procedures apply for stockholders to nominate candidates for election as directors or to bring matters before an annual meeting of stockholders.

If securities or industry analysts do not publish research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about us or our business. If one or more of the analysts who cover us downgrade our common stock or publish inaccurate or unfavorable research about our business, our common stock price would likely decline. If one or more of these analysts cease coverage of us or fail to publish reports on us regularly, demand for our common stock could decrease, which might cause our common stock price and trading volume to decline.

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ITEM 1B. UNRESOLVED STAFF COMMENTS
None.

ITEM 2. PROPERTIES
Our corporate headquarters are located in San Francisco, California, where we occupy facilities totaling approximately 43,000 square feet under a lease which expires in July 2022. We use these facilities for administration, sales and marketing, research and development, engineering, customer support and professional services. We also lease office space in Austin, Chicago and New York in the United States, and Australia, England, France, Germany, Ireland, Japan, and Singapore, which we use principally for sales and marketing, administration, customer support and to deliver professional services locally. We also lease office space in Portland, Oregon and Shanghai, China, which we use principally for engineering. We operate two data centers at third-party facilities located in the United States and Ireland.

We believe our facilities are in good condition and adequate for our current needs and for the foreseeable future. See Note 15 to the Consolidated Financial Statements and Management s Discussion and Analysis of Financial Condition and Results of Operations Contractual Obligations and Commitments for information regarding our lease obligations.

ITEM 3. LEGAL PROCEEDINGS
From time to time, we may become involved in legal proceedings arising in the ordinary course of our business. We are not presently a party to any legal proceedings that, if determined adversely to us, would individually or taken together have a material adverse effect on our business, operating results, financial condition or cash flows.

ITEM 4. MINE SAFETY DISCLOSURES
Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES
Market Price of Our Common Stock

Our common stock has traded on the New York Stock Exchange (NYSE) since March 22, 2013, under the symbol MRIN. Prior to this date, there was no public market for our common stock. The following tables set forth, for the periods indicated, the high and low sales price of our common shares as reported by the NYSE.

	High	Low
Year Ended December 31, 2014		
First Quarter	$ 12.57	$ 9.17

Second Quarter	$ 12.65	$ 8.41
Third Quarter	$ 12.14	$ 7.30
Fourth Quarter	$ 9.68	$ 7.79

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	High	Low
Year Ended December 31, 2013		
First Quarter (from March 22, 2013)	$ 19.95	$ 15.15
Second Quarter	$ 16.43	$ 8.75
Third Quarter	$ 14.37	$ 10.22
Fourth Quarter	$ 12.84	$ 8.50

Holders of our Common Shares

As of January 31, 2015, there were 114 stockholders of record. The actual number of stockholders is greater than the number of record holders, and includes stockholders who are beneficial owners, but whose shares are held in street name by brokers and other nominees. The number of holders of record also does not include stockholders whose shares may be held in trust by other entities.

Dividend Policy

We have never declared or paid any cash dividends on our common stock. We currently intend to retain any future earnings and do not expect to pay any cash dividends on our common stock for the foreseeable future. Any determination to pay dividends in the future will be at the discretion of our board of directors and will be dependent on a number of factors, including our earnings, capital requirements and overall financial conditions. In addition, the terms of our equipment loan agreement with Silicon Valley Bank currently restrict our ability to pay dividends.

Securities Authorized for Issuance under Equity Compensation Plans

The information required by this item will be set forth under the heading Equity Compensation Plan Information in the definitive Proxy Statement for our 2015 Annual Meeting of Stockholders (the Proxy Statement and is incorporated into this report by reference.

Unregistered Sales of Equity Securities

We made no sales of unregistered securities during the quarter ended December 31, 2014.

Use of Proceeds from Public Offering of Common Stock

There have been no material changes in our use of the proceeds from our initial public offering in March 2013.

Recent Issuer Purchases of Equity Securities

The table below provides information with respect to recent repurchases of unvested shares of our common stock.

Period	Total Number of Shares Purchased (1)	Weighted Average Price Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or	Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs

				Programs
October 1 October 31, 2014	555	$	2.58	
November 1 November 30, 2014	1,320	$	7.55	
December 1 December 31, 2014	0		N/A	

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(1) Certain of our shares of our common stock held by employees and service providers are subject to vesting. Unvested shares are subject to a right of repurchase by us in the event the holder of such shares is no longer employed by or providing services for us. All shares in the above table were shares repurchased as a result of our exercising this right and not pursuant to a publicly announced plan or program.

Stock Performance Graph

The following shall not be deemed filed for purposes of Section 18 of the Exchange Act, or incorporated by reference into any of our other filings under the Exchange Act or the Securities Act of 1933, as amended, except to the extent we specifically incorporate it by reference into such filing.

The following graph shows a comparison from March 22, 2013 (the date our common stock commenced trading on the NYSE) through December 31, 2014, of the cumulative total return for our common stock, the NYSE Composite Index, and the S&P 1500 Data Processing & Outsourced Services Index. The graph assumes an investment of $100 on March 22, 2013 and reinvestment of any dividends. The comparisons in the graph below are required by the Securities and Exchange Commission and are not intended to forecast or be indicative of possible future performance of our common shares.

Company / Index	3/22/13	3/31/13	6/30/13	9/30/13	12/31/13	3/31/14	6/30/14	9/30/14	12/31/14
Marin Software Inc.	**100**	117.36	73.14	89.64	73.14	75.50	84.07	61.43	60.43
NYSE Composite Index	**100**	100.51	101.83	107.58	116.92	119.07	125.00	122.55	124.81
S&P 1500 Data Processing & Outsourced Services	**100**	103.82	109.57	121.07	141.48	135.24	136.28	137.51	159.17

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ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following tables present selected historical financial data for our business. You should read this information together with Management s Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements, related notes and other financial information included elsewhere in this Annual Report on Form 10-K. The selected consolidated financial data in this section are not intended to replace the consolidated financial statements and are qualified in their entirety by the consolidated financial statements and related notes included elsewhere in this Annual Report on Form 10-K.

We derived the consolidated statements of operations data for the years ended December 31, 2014, 2013 and 2012, and the consolidated balance sheet data as of December 31, 2014 and 2013 from our audited consolidated financial statements included elsewhere in this report. We derived the consolidated statements of operations data for the years ended December 31, 2011 and 2010 and the consolidated balance sheet data as of December 31, 2012, 2011 and 2010 from our audited financial statements not included in this report. Our historical results are not necessarily indicative of the results to be expected in the future.

	Years Ended December 31,				
	2014	**2013**	**2012**	**2011**	**2010**
	(in thousands, except per share data)				
Revenues, net	$ 99,354	$ 77,315	$ 59,558	$ 36,121	$ 19,005
Cost of revenues (1)(2)	35,614	31,109	24,764	18,691	11,040
Gross profit	63,740	46,206	34,794	17,430	7,965
Operating expenses					
Sales and marketing (1)(2)	47,716	42,799	32,633	20,357	8,884
Research and development (1)(2)	28,751	20,715	14,014	7,071	4,568
General and administrative (1)(2)	21,257	17,028	13,432	6,679	5,195
Total operating expenses	97,724	80,542	60,079	34,107	18,647
Loss from operations	(33,984)	(34,336)	(25,285)	(16,677)	(10,682)
Interest expense, net	(177)	(453)	(520)	(378)	(230)
Other (expenses) income, net	(466)	(571)	(456)	(229)	78
Loss before benefit from (provision for) income taxes	(34,627)	(35,360)	(26,261)	(17,284)	(10,834)
Benefit from (provision for) income taxes	1,456	(492)	(221)	(139)	(23)
Net loss	(33,171)	(35,852)	(26,482)	(17,423)	(10,857)
Redemption of preferred stock in connection with the Series D financing and deemed dividend					(1,033)
Net loss available to common stockholders	$ (33,171)	$ (35,852)	$ (26,482)	$ (17,423)	$ (11,890)
Net loss per share available to common stockholders, basic and diluted (3)	$ (0.97)	$ (1.36)	$ (6.00)	$ (4.29)	$ (3.27)

Weighted-average shares used to compute net loss per share available to common stockholders, basic and diluted (3)	34,210	26,312	4,417	4,058	3,639

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(1) Stock-based compensation included in the consolidated statements of operations data above was allocated as follows:

	Years Ended December 31,				
	2014	2013	2012	2011	2010
	(in thousands)				
Cost of revenues	$ 765	$ 887	$ 439	$ 165	$ 90
Sales and marketing	1,895	1,304	1,005	226	66
Research and development	3,785	1,346	831	163	58
General and administrative	2,797	1,681	2,673	143	1,172
	$ 9,242	$ 5,218	$ 4,948	$ 697	$ 1,386

(2) Amortization of intangible assets included in the consolidated statements of operations data above was allocated as follows:

	Years Ended December 31,				
	2014	2013	2012	2011	2010
	(in thousands)				
Cost of revenues	$ 399	$	$	$	$
Sales and marketing	261				
Research and development	397				
General and administrative	74				
	$ 1,131	$	$	$	$

(3) See Note 13 of the consolidated financial statements for an explanation of the calculations of basic and diluted net loss per share available to common stockholders.

	As of December 31,				
	2014	2013	2012	2011	2010
	(in thousands)				
Consolidated Balance Sheet Data					
Cash and cash equivalents	$ 68,253	$ 104,407	$ 31,540	$ 1,719	$ 1,172
Property and equipment, net	16,274	14,417	9,224	4,909	3,113
Total assets	128,217	137,377	57,224	18,297	10,653
Debt, current and long-term	3,208	6,215	10,815	6,629	3,195
Convertible preferred stock, net of issuance costs			105,710	51,514	35,580
	106,117	115,344	(72,706)	(48,408)	(32,578)

Total stockholders equity (deficit)	

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ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this Annual Report on Form 10-K. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those forward-looking statements below. Factors that could cause or contribute to those differences include, but are not limited to, those identified below and those discussed in the section entitled Risk Factors included elsewhere in this Annual Report on Form 10-K. This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). These statements are often identified by the use of words such as believe, may, potentially, will, estimate, continue, anticipate, intend, could, would, project, plan, expect, seek, and similar expressions or variations. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified herein, and those discussed in the section titled Risk Factors , set forth in Part I, Item 1A of this Annual Report on Form 10-K. Except as required by law, we disclaim any obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We provide a leading cross-channel advertising cloud platform that enables digital marketers to improve performance of their online advertising campaigns, realize efficiencies and time savings, and make better business decisions. Our integrated platform is a software-as-a-service (SaaS) analytics, workflow, and optimization solution for marketing professionals, allowing them to effectively manage their digital advertising spend across search, display, social and mobile advertising channels. Our software solution is designed to help our customers:

- measure the effectiveness of their advertising campaigns through our proprietary reporting and analytics capabilities;
- manage and execute campaigns through our intuitive user interface and underlying technology that streamlines and automates key functions, such as ad creation and bidding, across multiple publishers and channels; and
- optimize campaigns across multiple publishers and channels in real time based on market and business data to achieve desired revenue outcomes using our predictive bid management technology.

In December 2014, our customers collectively managed more than $7.2 billion in annualized advertising spend on our platform and for the quarter ended December 31, 2014, we had 818 active advertisers using our solution globally across a wide range of industries. We market and sell our solutions to advertisers directly and through leading advertising agencies. For 2014, 2013 and 2012, our revenues were $99.4 million, $77.3 million and $59.6 million, representing period-over-period growth of 29%, 30% and 65%, respectively. We had net losses of $33.2 million in 2014, $35.9 million in 2013, and $26.5 million in 2012.

We earn revenues principally from subscription contracts under which we provide advertisers with access to our search, social and display advertising management platforms, either directly or through the advertiser s relationship with an agency that has a contract with us. In accordance with the subscription contracts, we charge fees generally based upon the amount of advertising spend that our customers manage through our platform. Our contracts are generally one year or longer in length. Under our subscription contracts with most of our direct advertisers and some of our agency customers, customers are contractually committed to a monthly minimum fee, which is payable on a monthly basis over the duration of the contract and is generally greater than one-half of our estimated monthly revenues from these customers, at the time the contract is signed. However, most of our

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subscription contracts with our advertising agency customers do not include a committed monthly minimum fee. Our contractual arrangement is with the advertising agency and the advertiser is not a party to the terms of the contract. Accordingly, most advertisers through our agency customers do not have a commitment to use our services and the advertisers may be added or removed from our platform at the discretion of the respective agency. We invoice the advertising agency for the amounts due under the contract. Historically, approximately half of our revenues have been earned from advertising agency customers. Our subscription fee under most contracts is variable based upon the value of advertising spend that our customers manage through our platform. Our deferred revenues consist of the unearned portion of billed subscription fees.

Our subscription contracts indicate the date at which we begin invoicing our customers, which is generally the first day of the month following the execution of the contract. We generally invoice the greater of the minimum fee or the percentage of advertising spend on our platform. The implementation process for new advertisers is typically four to six weeks; however, we generally do not charge a separate implementation fee under our subscription contracts.

Our implementation and customer support personnel, as well as costs associated with our operating infrastructure, are included in our cost of revenues. Our cost of revenues and operating expenses have increased in absolute dollars due to our need to increase our headcount to grow our business and to increase data center capacity to support customer revenue growth on our platform. We expect that our cost of revenues will continue to increase in absolute dollars as we continue to invest in our growth.

In order to grow revenues, we need to invest in (1) sales and marketing activities by adding sales and customer success representatives globally to target new advertisers and agencies and (2) research and development to further expand our platform and support for additional publishers. These activities will require us to make investments, particularly in research and development and sales and marketing, and if these investments do not generate additional customers or additional advertising spend managed by our platform, our future operating results could be harmed.

The majority of our revenues are derived from our advertisers in the United States. We believe the markets outside of the United States offer an opportunity for growth, and we intend to make additional investments in sales and marketing to expand in these markets. Advertisers from outside of the United States represented 34%, 32% and 27% of total revenues for 2014, 2013 and 2012, respectively.

We were incorporated in 2006 and initially focused on building the core elements of our cloud-based platform, which we currently use to service our customers. In September 2007, we launched Marin Enterprise, which targets large advertisers and agencies. We released Marin Professional Edition in March 2011, which targets mid-market advertisers and agencies. We have an iterative development process and we typically release new features every one to two months. Additionally, we have continued to expand internationally, opening our London office in 2009, our Paris, Hamburg, Singapore and Sydney offices in 2011, our Dublin and Tokyo offices in 2012 and our Shanghai office in 2013.

We completed our acquisition of NowSpots, Inc., which conducted business as Perfect Audience (Perfect Audience) in June 2014 to complement our product offerings, which is more fully described in Note 3 to our accompanying Consolidated Financial Statements. In February 2015, we completed our acquisition of SocialMoov to provide us with innovative social advertising technologies that will augment our current social offering, which is further described in Note 18 to our accompanying Consolidated Financial Statements.

Key Metrics

We regularly review a number of metrics to evaluate growth trends, measure our performance, establish budgets and make strategic decisions. Our selected key metrics include revenue, gross margin, operating expenses, active advertisers, annualized advertising spend on our platform and revenue retention rate. We discuss revenue, gross margin and operating expenses below under Components of Results of Operations. We monitor our key metrics to measure our success. Our revenues are generally based on the amount of advertising spend our customers manage on our platform in a period. As a result, revenues are an important metric to understanding the overall health of our business, and we use revenue trends to formulate financial projections and make strategic business decisions.

Number of Active Advertisers

We define an active advertiser as an advertiser from whom we recognized revenues in excess of $2,000 in at least one month in a period. We believe the $2,000 threshold best identifies advertisers who are actively using our platform. We focus on revenues in at least one month in a period to account for seasonality in advertising spend by our customers, some of whom may not run digital advertising campaigns in every month of a year but still represent an active advertiser on our platform. We count organizations within the same corporate structure as one advertiser, even if they have signed separate contracts with us for different brands or divisions, whether they are a direct advertiser or an advertiser through an agency. When our subscription contract is with an advertising agency, we include each advertiser whose advertising spend is managed by the agency through our platform as a different advertiser. Advertisers who have advertising spend managed by multiple agencies on our platform are counted as one advertiser. We believe that our ability to increase the number of active advertisers using our platform is a leading indicator of our ability to grow revenues. We had 818, 673 and 531 active advertisers in the quarters ending December 31, 2014, 2013 and 2012, respectively. While our active advertiser count has increased over time, this metric can also fluctuate from quarter to quarter due to seasonality and timing and amount of revenue contributed from new active advertisers and therefore, there is not necessarily a direct correlation between the amount of increased revenues and the change in active advertisers in a particular period.

Revenue Retention Rate

We believe our ability to retain and grow revenues from our existing advertisers is an indicator of the stability of our revenue base and the long-term value of our advertiser relationships. We assess our ability to retain and grow subscription revenues using a metric we refer to as revenue retention rate. We calculate our revenue retention rate metric by dividing retained revenues by retention base revenues. We define retention base revenues as revenues from all advertisers in the corresponding prior period, and we define retained revenues as revenues from all advertisers from the prior period that remain advertisers in the current period. This metric is calculated on a quarterly basis, and for annual periods, we use an average of the quarterly metrics. Although we have lost individual advertisers over time, advertisers who have remained on our platform have generally, in the aggregate, increased their advertising spend on our platform. At the same time, advertising spend on our platform may vary quarter to quarter, and as a result, quarterly revenue retention rates may fluctuate quarter to quarter. Our annual revenue retention rates were 97%, 97% and 114% in 2014, 2013 and 2012, respectively.

Annualized Advertising Spend on our Platform

We calculate annualized advertising spend as advertising spend in the last month of a period multiplied by 12. We believe that increases in annualized advertising spend generally lead to increases in revenues over time. However, we believe that other factors related to the terms of customer agreements and seasonality can make it difficult to directly correlate annual advertising spend to changes in revenues in a particular period. Our customers collectively managed $7.2 billion, $6.0 billion and $4.7 billion in annualized advertising spend on our platform in December 2014, 2013 and 2012, respectively.

Components of Results of Operations

Revenues

We generate revenues principally from subscription contracts under which we provide advertisers with access to our search, social and display advertising management platform, either directly or through the advertiser s relationship with an agency with whom we have a contract. Under our subscription contracts with most direct advertisers and some of our agency customers, customers contractually commit to a monthly minimum fee, which is generally greater than one-half of our estimated monthly revenues from these customers, at the time the contract is signed. However, most of our subscription contracts with our advertising agency customers do not include a committed monthly minimum fee. Additionally, advertisers we serve through our arrangements with our advertising agencies generally do not have a minimum commitment to continue using our services. Our subscription fee under most contracts is variable based upon the value of advertising spend that our customers manage through our platform, although some customers pay a flat monthly rate over the term of their subscription contract. Our deferred revenues consist of the unearned portion of billed subscription fees.

Cost of Revenues

Cost of revenues primarily includes personnel costs, consisting of salaries, benefits, bonuses and stock-based compensation, for employees associated with our cloud infrastructure and global services for implementation and ongoing customer service organizations. Other costs of revenues include fees paid to contractors who supplement our support and data center personnel, expenses related to the use of a third-party data center, depreciation of data center equipment, amortization of capitalized internal-use software development costs, amortization of intangible assets and allocated overhead.

We intend to continue to invest additional resources in our global services teams and in the capacity of our hosting service infrastructure. As we continue to invest in technology innovation through our research and development organization, we expect to have increased amortization of capitalized internal-use software development costs. We expect that this investment in technology should not only expand the breadth and depth of our cross-channel performance advertising cloud platform but also increase the efficiency of how we deliver these solutions, enabling us to improve our gross margin over time. The level and timing of investment in these areas could affect our cost of revenues in the future.

Sales and Marketing Expenses

Sales and marketing expenses include personnel costs, sales commissions and other costs including travel and entertainment, marketing and promotional events, public relations, marketing activities, professional fees and allocated overhead. All of these costs are expensed as incurred, including sales commissions. Our commission plans provide that payment of commissions to our sales representatives are paid based on the actual amounts we invoice customers over a period that is generally up to five months following the execution of the applicable customer contract.

We plan to continue investing in sales and marketing by increasing the number of sales and account management employees, expanding our domestic and international sales and marketing activities, building brand awareness and sponsoring additional marketing events, which we believe will enable us to add new customers and increase penetration within our existing customer base. We expect that, in the future, sales and marketing expenses will increase in absolute dollars and continue to be our largest operating expense category.

Research and Development Expenses

Research and development expenses consist primarily of personnel costs for our product development and engineering employees and executives, including salaries, benefits, stock-based compensation expense and bonuses. Also included are non-personnel costs such as professional fees payable to third-party development resources, amortization of intangible assets and allocated overhead.

Our research and development efforts are focused on enhancing our software architecture, adding new features and functionality to our platform and improving the efficiency with which we deliver these services to our customers. We expect that, in the future, research and development expenses will increase in absolute dollars, partially offset by the capitalization of internal-use software development costs. We believe that these investments are necessary to maintain and improve our competitive position.

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General and Administrative Expenses

General and administrative expenses consist primarily of personnel costs, including salaries, benefits, stock-based compensation expense and bonuses, for our administrative, legal, human resources, finance and accounting employees and executives. Also included are non-personnel costs, such as travel-related expenses, audit fees, tax services and legal fees, as well as professional fees, insurance and other corporate expenses, along with amortization of intangible assets and allocated overhead.

We expect to incur incremental costs associated with supporting the growth of our business, both in terms of size and geographic expansion, and to meet the increased compliance requirements associated with our continued operation as a public company. Such costs include increases in our accounting and legal personnel, additional consulting, legal and audit fees, insurance costs, board of directors compensation and the costs of achieving and maintaining compliance with the Sarbanes-Oxley Act of 2002. As a result, we expect our general and administrative expenses to increase in absolute dollars in future periods but to decrease as a percentage of revenues over time.

Other Expenses, Net and Interest Expenses, Net

Other expenses, net primarily consists of foreign currency transaction gains and losses. Interest expense, net, consists primarily of interest income earned on our cash equivalents offset by the interest expense for our capital lease payments and borrowings under our equipment advances and revolving line of credit.

Benefit from (Provision for) Income Taxes

The benefit from (provision for) income taxes consists of federal, state and foreign income taxes. Due to recent losses, we maintain a valuation allowance against our deferred tax assets as of December 31, 2014. We consider all available evidence, both positive and negative, in assessing the extent to which a valuation allowance should be applied against our deferred tax assets.

Results of Operations

The following table is a summary of our consolidated statements of operations. The period-to-period comparisons of results are not necessarily indicative of results for future periods.

	Years Ended December 31,		
	2014	2013	2012
	(in thousands)		
Revenues, net	$ 99,354	$ 77,315	$ 59,558
Cost of revenues (1)(2)	35,614	31,109	24,764
Gross profit	63,740	46,206	34,794
Operating expenses			
Sales and marketing (1)(2)	47,716	42,799	32,633
Research and development (1)(2)	28,751	20,715	14,014
General and administrative (1)(2)	21,257	17,028	13,432

Total operating expenses	97,724	80,542	60,079
Loss from operations	(33,984)	(34,336)	(25,285)
Interest expense, net	(177)	(453)	(520)
Other expenses, net	(466)	(571)	(456)
Loss before benefit from (provision for) income taxes	(34,627)	(35,360)	(26,261)
Benefit from (provision for) income taxes	1,456	(492)	(221)
Net loss	$ (33,171)	$ (35,852)	$ (26,482)

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(1) Stock-based compensation included in the consolidated statements of operations data above was as follows:

	Years Ended December 31,		
	2014	2013	2012
	(in thousands)		
Cost of revenues	$ 765	$ 887	$ 439
Sales and marketing	1,895	1,304	1,005
Research and development	3,785	1,346	831
General and administrative	2,797	1,681	2,673
	$ 9,242	$ 5,218	$ 4,948

(2) Amortization of intangible assets included in the consolidated statements of operations data above was as follows:

	Years Ended December 31,		
	2014	2013	2012
	(in thousands)		
Cost of revenues	$ 399	$	$
Sales and marketing	261		
Research and development	397		
General and administrative	74		
	$ 1,131	$	$

The following table sets forth our consolidated results of operations for the specified periods as a percentage of our revenues for those periods. Percent of revenue figures are rounded and therefore may not subtotal exactly.

	Years Ended December 31,		
	2014	2013	2012
Revenues, net	100%	100%	100%
Cost of revenues	36	40	42
Gross profit	64	60	58
Operating expenses			
Sales and marketing	48	55	55
Research and development	29	27	24
General and administrative	21	22	23
Total operating expenses	98	104	101

Loss from operations	(34)	(44)	(42)
Interest expense		(1)	(1)
Other expenses, net		(1)	(1)
Loss before benefit from (provision for) income taxes	(35)	(46)	(44)
Benefit from (provision for) income taxes	1	(1)	
Net loss	(33)%	(46)%	(44)%

The following tables set forth our consolidated revenues by geographic area:

	Years Ended December 31,		
	2014	2013	2012
		(in thousands)	
Revenues, net by geography			
United States of America	$ 65,745	$ 52,725	$ 43,429
International	33,609	24,590	16,129
Total revenues, net	$ 99,354	$ 77,315	$ 59,558

	Years Ended December 31,		
	2014	2013	2012
Revenues, net by geography			
United States of America	66%	68%	73%
International	34	32	27
Total revenues, net	100%	100%	100%

Adjusted EBITDA

Adjusted EBITDA is a financial measure that is not calculated in accordance with generally accepted accounting principles in the United States (GAAP). We define Adjusted EBITDA as net loss, adjusted for stock-based compensation expense, depreciation, the amortization of internally developed software, the amortization of intangible assets, the capitalization of internally developed software, interest expense, net, the benefit from or provision for income taxes, other income or expenses, net, and the non-recurring costs associated with acquisitions. Adjusted EBITDA is a financial measure that is not calculated in accordance with GAAP. We believe Adjusted EBITDA is useful to investors in evaluating our operating performance for the following reasons:

Adjusted EBITDA is widely used by investors and securities analysts to measure a company s operating performance without regard to items, such as stock-based compensation expense, depreciation and amortization, capitalized software development costs, interest expense, net, benefit from or provision for income taxes, other income or expenses, net and non-recurring costs associated with acquisitions, that can vary substantially from company to company depending upon their financing, capital structures and the method by which assets were acquired;

Our management uses Adjusted EBITDA in conjunction with GAAP financial measures for planning purposes, including the preparation of our annual operating budget, as a measure of operating performance and the effectiveness of our business strategies and in communications with our board of directors concerning our financial performance; and

Adjusted EBITDA provides consistency and comparability with our past financial performance, facilitates period-to-period comparisons of operations and also facilitates comparisons with other peer companies, many of which use similar non-GAAP financial measures to supplement their GAAP results.

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 you should not consider it in isolation or as a substitute for analysis of our results of operations as reported under GAAP. These limitations include:

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;

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Adjusted EBITDA does not reflect changes in, or cash requirements for, our working capital needs or contractual commitments;

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

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

The following table presents a reconciliation of net loss, the most comparable GAAP measure, to Adjusted EBITDA for each of the periods indicated:

	Years Ended December 31,		
	2014	2013	2012
		(in thousands)	
Net loss	$ (33,171)	$ (35,852)	$ (26,482)
Depreciation	5,669	4,722	2,642
Amortization of internally developed software	1,905	1,156	525
Amortization of intangible assets	1,131		
Interest expense, net	177	453	520
(Benefit from) provision for income taxes	(1,456)	492	221
EBITDA	(25,745)	(29,029)	(22,574)
Stock-based compensation expense	9,242	5,218	4,948
Capitalization of internally developed software	(3,146)	(3,216)	(1,743)
Acquisition related expenses	351		
Other expenses, net	466	571	456
Adjusted EBITDA	$ (18,832)	$ (26,456)	$ (18,913)

Comparison of the Years Ended December 31, 2014 and 2013

Revenues

	Years Ended December 31,		Change	
	2014	2013	$	%
		(dollars in thousands)		
Total revenues, net	$ 99,354	$ 77,315	$ 22,039	29%

Revenues increased $22.0 million, or 29%, for 2014 as compared to 2013. This increase was driven primarily by growth in revenues from both new and existing advertisers in all geographies as our ongoing investment in sales and marketing resources resulted in increased demand for our platform worldwide. During the year, we also began to generate revenues from advertisers who utilized our newly acquired display re-targeting functionalities. During 2014, we generated $13.4 million of revenue from new advertisers, and $8.6 million of additional revenue from our existing advertisers. We define a new advertiser as an advertiser from whom we earned revenue during the current fiscal period and from whom we did not earn any revenue during the immediately prior fiscal period. There were no customers that accounted for greater than 10% of our revenues in 2014 or 2013.

Revenues in 2014 from the United States, United Kingdom and other international locations represented 66%, 10% and 24%, respectively, of revenues, and in 2013, revenues from the United States, United Kingdom and other international locations represented 68%, 9% and 23%, respectively, of revenues.

Cost of Revenues and Gross Margin

	Years Ended December 31, 2014	2013	Change $	%
	(dollars in thousands)			
Cost of revenues	$ 35,614	$ 31,109	$ 4,505	14%
Gross profit	63,740	46,206	17,534	38
Gross margin	64%	60%		

Cost of revenues increased $4.5 million, or 14%, as compared to 2013. This primarily results from increases of $1.5 million in depreciation and amortization expense (related to internally developed software) and $1.2 million in hosting costs to support the increased use of our hosted platform, as well as an increase of $0.9 million in compensation and benefits expenses and $0.4 million of allocated overhead, resulting from an increase in the average number of global services and platform infrastructure personnel during 2014. Amortization of intangible assets acquired as part of the acquisition of Perfect Audience in June 2014 amounted to $0.4 million for the year ended December 31, 2014.

Our gross margin increased to 64% during 2014 from 60% during 2013. This increase was due to the achievement of greater operational efficiency from personnel dedicated to our cloud infrastructure and global services precipitated by upgraded functionality and capabilities delivered by our engineering team.

Sales and Marketing

	Years Ended December 31, 2014	2013	Change $	%
	(dollars in thousands)			
Sales and marketing	$ 47,716	$ 42,799	$ 4,917	11%
Percent of revenues, net	48%	55%		

Sales and marketing expenses increased $4.9 million, or 11%, as compared to 2013. The increases were primarily due to an increase our average global sales and marketing headcount during 2014, contributing to an increase of $3.9 million in personnel-related costs, consisting primarily of increased employee compensation, benefits and travel costs associated with our sales force. The remaining $1.0 million increase during 2014 is primarily the result of an increase in allocated overhead of $0.6 million due to the growth in headcount relative to the rest of our company, and amortization expense of $0.3 million related to intangible assets acquired as part of the acquisition of Perfect Audience in June 2014.

Research and Development

	Years Ended December 31, 2014	2013	Change $	%
	(dollars in thousands)			
Research and development	$ 28,751	$ 20,715	$ 8,036	39%
Percent of revenues, net	29%	27%		

Research and development expenses increased $8.0 million, or 39%, as compared to 2013. This primarily reflected an increase in average research and development headcount during 2014, resulting in an increase of $6.9 million in compensation expense. During 2014, allocated overhead increased $0.6 million due to the increase in headcount, and amortization of intangible assets acquired as part of the acquisition of Perfect Audience in June 2014 amounted to $0.4 million.

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General and Administrative

	Years Ended December 31,		Change	
	2014	2013	$	%
	(dollars in thousands)			
General and administrative	$ 21,257	$ 17,028	$ 4,229	25%
Percent of revenues, net	21%	22%		

General and administrative expenses increased $4.2 million, or 25%, respectively, as compared to 2013. Compensation, benefits and other employee-related expenses exclusive of stock-based compensation increased by $2.3 million, as we added employees to support the growth of our business. Professional fees and insurance expenses increased $1.0 million to support our global expansion and the acquisition of Perfect Audience in June 2014. Bad debt expense increased $0.5 million, which was relatively in line with the corresponding increase in sales from 2013 to 2014. We also incurred $0.3 million in costs directly related to the acquisition of Perfect Audience in June 2014.

Other Expenses, Net and Interest Expense, Net

	Years Ended December 31,		Change	
	2014	2013	$	%
	(dollars in thousands)			
Other expenses, net and interest expense, net	$ (643)	$ (1,024)	$ (381)	(37)%

Other expenses, net primarily consists of foreign currency transaction gains and losses. The decrease of $0.4 million, or 37%, in other expenses, net, and interest expense, net, during 2014 was primarily due to a decrease of $0.3 million in interest expense as we continued to pay down our long-term debt, partially offset by an increase of $0.2 million in foreign exchange losses due to the growth of our international operations and fluctuations in foreign currency exchange rates. Other expenses, net, during 2014 also excluded $0.2 million in losses resulting from the change in the fair value of freestanding preferred stock warrants incurred during 2013. Upon the consummation of the Company s initial public offering (IPO), those warrants converted into warrants to purchase common stock and were reclassified from liabilities to additional paid-in capital. As a result, changes in their fair value are no longer recorded on the consolidated statement of comprehensive loss.

Benefit from (Provision for) Income Taxes

	Years Ended December 31,		Change	
	2014	2013	$	%
	(dollars in thousands)			
Benefit from (provision for) income taxes	$ 1,456	$ (492)	$ 1,948	(396)%

Benefit from income taxes for 2014 increased $1.9 million primarily due to a decrease in our valuation allowances of $2.3 million as a result of deferred tax liabilities recorded as part of our acquisition of Perfect Audience in June 2014. This increased benefit was partially offset by additional provision for income taxes due to increased profits generated in foreign jurisdictions by our wholly-owned subsidiaries.

Comparison of the Years Ended December 31, 2013 and 2012

Revenues

	Years Ended December 31,		Change	
	2013	**2012**	**$**	**%**
	(dollars in thousands)			
Revenues	$ 77,315	$ 59,558	$ 17,757	30%

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Revenues increased $17.8 million, or 30%, for 2013 as compared to 2012. This increase was driven by growth in revenues from both new and existing advertisers in all geographies as our ongoing investment in sales and marketing resources resulted in increased demand for our platform worldwide. During 2013, we generated $11.1 million of revenue from new advertisers and $6.7 million of additional revenue from our existing advertisers. We define a new advertiser as an advertiser from whom we earned revenue during the current fiscal period and from whom we did not earn any revenue during the previous corresponding period. There were no customers that accounted for greater than 10% of our revenues in 2013 or 2012.

Revenues in 2013 from the United States and international locations represented 68% and 32%, respectively, of revenues, and in 2012, revenues from the United States and international locations represented 73% and 27%, respectively, of revenues.

Cost of Revenues and Gross Margin

	Years Ended December 31,		Change	
	2013	2012	$	%
	(dollars in thousands)			
Cost of revenues	$ 31,109	$ 24,764	$ 6,345	26%
Gross profit	46,206	34,794	11,412	33
Gross margin	60%	58%		

Cost of revenues increased $6.3 million, or 26%, as compared to 2012. This reflected an increase in the average number of global services and platform infrastructure personnel from 118 employees during 2012 to 135 employees during 2013, resulting in an increase of $2.7 million in compensation and benefits expenses and $0.1 million of allocated overhead. During 2013, we also experienced increases of $2.2 million in depreciation and amortization expense, $0.9 million in hosting costs, $0.3 million of equipment-related expenses, and $0.2 million of professional fees to support the increased use of our hosted platform.

Our gross margin increased to 60% during 2013 from 58% during 2012. This increase was due to the achievement of greater operational efficiency from personnel dedicated to our cloud infrastructure and global services precipitated by upgraded functionality and capabilities delivered by our engineering team. Compensation for these personnel was 23% of revenues during 2013, as compared to 25% during 2012.

Sales and Marketing

	Years Ended December 31,		Change	
	2013	2012	$	%
	(dollars in thousands)			
Sales and marketing	$ 42,799	$ 32,633	$ 10,166	31%
Percent of revenues, net	55%	55%		

Sales and marketing expenses increased $10.2 million, or 31%, as compared to 2012. The increases were primarily due to an increase our average global sales and marketing headcount from 123 employees during 2012 to 161 employees during 2013, contributing to an increase of $8.2 million in personnel-related costs, consisting primarily of increased employee compensation, benefits and travel costs associated with our sales force. Stock-based compensation during 2013 did not include $0.4 million in stock-based compensation incurred in 2012 directly attributable to the redemption of common shares from an employee for an amount above the fair value at the time of the redemption. Allocated overhead increased $0.8 million and recruiting fees increased $0.1 million, also due to the growth in headcount relative to the rest of our company. Marketing event and technology costs increased $0.7 million due to our continued marketing efforts and professional fees also increased $0.3 million during 2013.

Research and Development

	Years Ended December 31,		Change	
	2013	2012	$	%
	(dollars in thousands)			
Research and development	$ 20,715	$ 14,014	$ 6,701	48%
Percent of revenues, net	27%	24%		

Research and development expenses increased $6.7 million, or 48%, as compared to 2012. This reflected an increase in average research and development headcount from 88 employees during 2012 to 130 employees during 2013, resulting in an increase of $4.9 million in compensation expense. Stock-based compensation for 2013 did not include $0.3 million in stock-based compensation incurred in 2012 directly attributable to the redemption of common shares from two employees for an amount above the fair value at the time of the redemption. Allocated overhead also increased $1.1 million due to the increase in headcount. Professional fees increased $0.3 million to supplement our employees efforts to enhance our software architecture. Recruiting, equipment, and travel expenses increased $0.3 million in total to support the opening of our new office in Shanghai.

General and Administrative

	Years Ended December 31,		Change	
	2013	2012	$	%
	(dollars in thousands)			
General and administrative	$ 17,028	$ 13,432	$ 3,596	27%
Percent of revenues	22%	23%		

General and administrative expenses increased $3.6 million, or 27%, respectively, as compared to 2012. Included in this balance during 2012 is $1.9 million in stock-based compensation directly associated with the redemption of common shares from two employees for an amount above the fair value at the time of the redemption. As a result, stock-based compensation for general and administrative employees decreased $1.0 million during 2013. Excluding stock-based compensation, general and administrative expenses increased $4.6 million. Compensation, benefits and other employee-related expenses exclusive of stock-based compensation increased by $2.3 million, as we added employees to support the growth of our business and as we became a public company. Professional fees and insurance expenses increased $0.6 million and $0.4 million, respectively, to support our global expansion and as we completed our IPO and became a public company during the March 2013. Allocated overhead and recruiting fees increased $0.4 million and $0.2 million, respectively, to support our growth in headcount. Expenses for non-income based taxes increased $0.2 million as we became a public company. Banking fees also increased $0.2 million as we continued our international expansion.

Other Expenses, Net

	Years Ended December 31,		Change	

	2013	2012	$	%
	(dollars in thousands)			
Other expenses, net	($ 1,024)	($ 976)	($ 48)	5%

Other expenses, net primarily consists of foreign currency transaction gains and losses and interest expense. Interest expense decreased $0.1 million in 2013, as we paid off the balance on our revolving line of credit. Foreign currency transaction losses increased $0.1 million due to the growth of our international operations.

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Provision for Income Taxes

	Years Ended December 31,		Change	
	2013	2012	$	%
	(dollars in thousands)			
Provision for income taxes	$ 492	$ 221	$ 271	123%

Provision for income increased $0.3 million as a result of increased profits generated in foreign jurisdictions by our wholly-owned subsidiaries.

Quarterly Results of Operations

The following table sets forth our unaudited quarterly consolidated statements of operations data for each of the eight quarters in the period ended December 31, 2014. We have prepared the quarterly data on a basis consistent with our audited annual financial statements, including, in the opinion of management, all normal recurring adjustments necessary for the fair statement of the financial information contained in these statements. The historical results are not necessarily indicative of future results and should be read in conjunction with our consolidated financial statements and the related notes included elsewhere in this Annual Report on Form 10-K.

	Three Months Ended							
	December 31, 2014	September 30, 2014	June 30, 2014	March 31, 2014	December 31, 2013	September 30, 2013	June 30, 2013	March 31, 2013
	(in thousands)							
Revenues, net	$ 27,002	$ 25,684	$ 23,853	$ 22,815	$ 21,829	$ 20,113	$ 18,218	$ 17,155
Cost of revenues (1)(2)	9,323	9,145	8,763	8,383	8,097	7,944	7,696	7,372
Gross profit	17,679	16,539	15,090	14,432	13,732	12,169	10,522	9,783
Operating expenses								
Sales and marketing (1)(2)	11,563	12,186	11,978	11,989	11,709	10,281	10,350	10,459
Research and development (1)(2)	8,217	7,824	6,627	6,083	5,660	5,072	4,904	5,079
General and administrative (1)(2)	5,791	5,682	5,368	4,416	4,273	4,681	4,026	4,048
Total operating expenses	25,571	25,692	23,973	22,488	21,642	20,034	19,280	19,586
Loss from operations	(7,892)	(9,153)	(8,883)	(8,056)	(7,910)	(7,865)	(8,758)	(9,803)
Interest expense, net	(16)	(33)	(62)	(66)	(78)	(82)	(109)	(184)
	(385)	201	(286)	4	(66)	(16)	(81)	(408)

Other (expenses) income, net								
Loss before (provision for) benefit from income taxes	(8,293)	(8,985)	(9,231)	(8,118)	(8,054)	(7,963)	(8,948)	(10,395)
(Provision for) benefit from income taxes	(537)	(259)	2,440	(188)	(7)	(230)	(149)	(106)
Net loss	$ (8,830)	$ (9,244)	$ (6,791)	$ (8,306)	$ (8,061)	$ (8,193)	$ (9,097)	$ (10,501)
Net loss per share available to common stockholders, basic and diluted	$ (0.25)	$ (0.27)	$ (0.20)	$ (0.25)	$ (0.25)	$ (0.25)	$ (0.28)	$ (1.43)

(1) Stock-based compensation included in the consolidated statements of operations data above was as follows:

	Three Months Ended							
	December 31, 2014	**September 30, 2014**	**June 30, 2014**	**March 31, 2014**	**December 31, 2013**	**September 30, 2013**	**June 30, 2013**	**March 31, 2013**
	(in thousands)							
Cost of revenues	$ 189	$ 173	$ 192	$ 211	$ 198	$ 239	$ 245	$ 205
Sales and marketing	513	530	449	403	301	349	361	293
Research and development	1,337	1,362	649	437	356	379	303	308
General and administrative	849	851	651	446	411	451	400	419
Total stock-based compensation	$ 2,888	$ 2,916	$ 1,941	$ 1,497	$ 1,266	$ 1,418	$ 1,309	$ 1,225

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(2) Amortization of intangible assets included in the consolidated statements of operations data above was as follows:

	Three Months Ended							
	December 31, 2014	**September 30, 2014**	**June 30, 2014**	**March 31, 2014**	**December 31, 2013**	**September 30, 2013**	**June 30, 2013**	**March 31, 2013**
	(in thousands)							
Cost of revenues	$ 171	$ 171	$ 57	$	$	$	$	$
Sales and marketing	112	112	37					
Research and development	170	170	57					
General and administrative	32	32	10					
Total amortization of intangible assets	$ 485	$ 485	$ 161	$	$	$	$	$

&nbsze:10pt;">Warranty accrual $4,335 $4,181

Accrued compensation and benefits	4,169	5,106
Accrued interest	705	453
Income taxes payable	2,143	6,780
Deferred profit from unconsolidated joint ventures	1,062	1,603
Other accrued expenses	1,653	1,704
	$ 14,067	$ 19,827

Changes in our warranty accrual are detailed in the table set forth below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(Dollars in thousands)			
Beginning warranty accrual for homebuilding projects	$4,874	$1,902	$3,846	$1,277
Warranty provision for homebuilding projects	369	579	1,174	1,333
Warranty assumed from joint venture at consolidation	—	—	469	—
Warranty payments for homebuilding projects	(168)	(59)	(414)	(188)
Adjustment to warranty accrual	(1,065)	—	(1,065)	—
Ending warranty accrual for homebuilding projects	4,010	2,422	4,010	2,422
Beginning warranty accrual for fee building projects	331	297	335	301
Warranty provision for fee building projects	—	57	—	57
Warranty efforts for fee building projects	(6)	(14)	(10)	(18)
Ending warranty accrual for fee building projects	325	340	325	340

Total ending warranty accrual	$4,335	$2,762	$4,335	$2,762

During the third quarter of 2016, we recorded an adjustment of $1.1 million to our warranty accrual primarily due to lower than expected warranty related expenditures. The corresponding adjustment was included as a reduction to cost of home sales in the accompanying condensed consolidated statements of operations.

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THE NEW HOME COMPANY INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

8. Unsecured Revolving Credit Facility and Other Notes Payable

Notes payable consisted of the following:

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
Senior unsecured revolving credit facility	$229,924	$ 74,924
Note payable to land seller	4,000	6,000
Construction loans	—	2,158
	$233,924	$ 83,082

We have a senior unsecured revolving credit facility (the "Credit Facility") with a bank group. In May 2016, we increased the commitment under the Credit Facility from $200 million to $260 million with an accordion feature that allows borrowings thereunder to be increased up to an aggregate of $350 million and extended the maturity date by one year to April 30, 2019. As of September 30, 2016, we had $229.9 million outstanding under the credit facility and $30.1 million in availability. We may repay advances at any time without premium or penalty. Interest is payable monthly and is charged at a rate of 1-month LIBOR plus a margin ranging from 2.25% to 3.00% depending on the Company's leverage ratio as calculated at the end of each fiscal quarter. As of September 30, 2016, the interest rate under the Credit Facility was 3.28%. Pursuant to the Credit Facility, the Company is required to maintain certain financial covenants as defined in the Credit Facility, including (i) a minimum tangible net worth; (ii) leverage ratios; (iii) a minimum liquidity covenant; and (iv) a minimum fixed charge coverage ratio based on EBITDA (as detailed in the Credit Facility) to interest incurred. As of September 30, 2016, the Company was in compliance with all financial covenants.

The Company has a note payable to a land seller, secured by real estate, which bears interest at 7.0% per annum. As of September 30, 2016, the outstanding balance of the loan was $4.0 million and matures on the earlier of (i) 10 days following entitlement approval, or (ii) December 15, 2016. Interest is payable monthly and the remaining principal is due at maturity.

9. Fair Value Disclosures

ASC 820, Fair Value Measurements and Disclosures, defines fair value as the price that would be received for selling an asset or paid to transfer a liability in an orderly transaction between market participants at measurement date and requires assets and liabilities carried at fair value to be classified and disclosed in the following three categories:

- Level 1 – Quoted prices for identical instruments in active markets
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are inactive; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets at measurement date
- Level 3 – Valuations derived from techniques where one or more significant inputs or significant value drivers are unobservable in active markets at measurement date

Fair Value of Financial Instruments

The accompanying condensed consolidated balance sheets include the following financial instruments: cash and cash equivalents, restricted cash, contracts and accounts receivable, due from affiliates, accounts payable, accrued expenses and other liabilities, due to affiliates, unsecured revolving credit facility and other notes payable.

The Company considers the carrying value of cash and cash equivalents, restricted cash, contracts and accounts receivable, accounts payable, and accrued expenses and other liabilities to approximate the fair value of these financial instruments based on the short duration between origination of the instruments and their expected realization. The fair value of amounts due from affiliates and due to affiliates is not determinable due to the related party nature of such amounts. As of September 30, 2016 and December 31, 2015, the fair value of the Company's unsecured revolving credit facility and other notes payable approximated the carrying value. The Company has determined that its unsecured revolving credit facility and other notes payable are classified as Level 3 within the fair value hierarchy. The estimated fair value of the outstanding revolving credit facility balance at September 30, 2016 and December 31, 2015 approximated the carrying value due to the short-term nature of LIBOR contracts. The estimated fair value of other notes payable at September 30, 2016 and December 31, 2015 was based on a cash flow model discounted at market interest rates that considered underlying risks of the debt.

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THE NEW HOME COMPANY INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Non-Recurring Fair Value Adjustments

Nonfinancial assets and liabilities include items such as inventory and long-lived assets that are measured at cost when acquired and adjusted for impairment to fair value, if deemed necessary. During the three and nine months ended September 30, 2016 and 2015, the Company did not record any fair value adjustments to those nonfinancial assets and liabilities remeasured at fair value on a nonrecurring basis.

10. Commitments and Contingencies

The Company is a defendant in various lawsuits related to its normal course of business. We record a reserve for potential legal claims and regulatory matters when they are probable of occurring and a potential loss is reasonably estimable. We accrue for these matters based on facts and circumstances specific to each matter and revise these estimates when necessary.

In view of the inherent difficulty of predicting outcomes of legal claims and related contingencies, we generally cannot predict their ultimate resolution, related timing or eventual loss. If our evaluations indicate loss contingencies that could be material are not probable, but are reasonably possible, we will disclose their nature with an estimate of possible range of losses or a statement that such loss is not reasonably estimable. As of September 30, 2016 and December 31, 2015, the Company did not have any accruals for asserted or unasserted matters.

As an owner and developer of real estate, the Company is subject to various environmental laws of federal, state and local governments. The Company is not aware of any environmental liability that could have a material adverse effect on its financial condition or results of operations. However, changes in applicable environmental laws and regulations, the uses and conditions of real estate in the vicinity of the Company’s real estate and other environmental conditions of which the Company is unaware with respect to the real estate could result in future environmental liabilities.

The Company has provided credit enhancements in connection with joint venture borrowings in the form of LTV maintenance agreements in order to secure the joint venture's performance under the loans and maintenance of certain LTV ratios. The Company has also entered into agreements with its partners in each of the unconsolidated joint ventures whereby the Company and its partners are apportioned liability under the LTV maintenance agreements according to their respective capital interest. In addition, the agreements provide the Company, to the extent its partner has an unpaid liability under such credit enhancements, the right to receive distributions from the unconsolidated joint venture that would otherwise be made to the partner. However, there is no guarantee that such distributions will be made or will be sufficient to cover the share of the liability apportioned to us. The loans underlying the LTV maintenance agreements comprise acquisition and development loans, construction revolvers and model home loans, and the agreements remain in force until the loans are satisfied. Due to the nature of the loans, the outstanding balance at any given time is subject to a number of factors including the status of site improvements, the mix of horizontal and vertical development underway, the timing of phase build outs, and the period necessary to complete the escrow process for homebuyers. As of September 30, 2016 and December 31, 2015, $81.7 million and $74.1 million, respectively, was outstanding under the loans and credit enhanced by the Company through LTV maintenance agreements. Under the terms of the joint venture agreements, the Company's proportionate share of LTV maintenance agreement liabilities was $12.0 million and $22.5 million, respectively, as of September 30, 2016 and December 31, 2015. In addition, the Company has provided completion guaranties regarding specific performance for certain projects whereby the Company is required to complete the given project with funds provided by the beneficiary of the guaranty. If there are not adequate funds available under the specific project loans, the Company would then be subject to financial liability under such completion guaranties. Typically, under such terms of the joint venture agreements, the Company has the right to apportion the respective share of any costs funded under such completion guaranties to its partners. However, there is no guarantee that we will be able to recover against our partners for such amounts owed to us under the terms of such joint venture agreements.

We obtain surety bonds in the normal course of business to ensure completion of certain infrastructure improvements of our projects. As of September 30, 2016 and December 31, 2015, the Company had outstanding surety bonds totaling $48.2 million and $33.6 million, respectively. The estimated remaining costs to complete such improvements as of September 30, 2016 and December 31, 2015 were $15.5 million and $17.0 million, respectively. The beneficiaries of the bonds are various municipalities and other organizations. In the event that any such surety bond issued by a third party is called because the required improvements are not completed, the Company could be obligated to reimburse the issuer of the bond.

On May 6, 2015, the Company entered into a letter of credit facility agreement that allows the Company and certain affiliated unconsolidated joint ventures to issue up to $5.0 million in letters of credit. The agreement includes an option to increase this amount to $7.5 million, subject to certain conditions. As of September 30, 2016, our affiliated unconsolidated joint ventures had $3.6 million in outstanding letters of credit issued under this facility.

THE NEW HOME COMPANY INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

11. Related Party Transactions

During the three and nine months ended September 30, 2016 and 2015, the Company incurred construction-related costs on behalf of its unconsolidated joint ventures totaling $2.6 million, $7.0 million, $2.8 million and $8.6 million, respectively. As of September 30, 2016 and December 31, 2015, $0.3 million and $0.3 million, respectively, are included in due from affiliates in the accompanying condensed consolidated balance sheets.

The Company has entered into Management Agreements with its unconsolidated joint ventures to provide management services related to the underlying projects. Pursuant to the Management Agreements, the Company receives a management fee based on each project’s revenues. During the three and nine months ended September 30, 2016 and 2015, the Company earned $1.5 million, $6.3 million, $3.3 million and $8.4 million, respectively, in management fees, which have been recorded as fee building revenue in the accompanying condensed consolidated statements of operations. As of September 30, 2016 and December 31, 2015, $0.2 million and $0.7 million, respectively, of management fees are included in due from affiliates in the accompanying condensed consolidated balance sheets.

One member of the Company's board of directors beneficially owns more than 10% of the Company's outstanding common stock through an affiliated entity and is also affiliated with an entity that has investments in two of the Company's unconsolidated joint ventures. As of September 30, 2016, the Company's investment in these two unconsolidated joint ventures totaled $10.2 million.

TL Fab LP, an affiliate of Paul Heeschen, one of the Company's non-employee directors, was engaged by the Company and some of its unconsolidated joint ventures as a trade contractor to provide metal fabrication services. For the three and nine months ended September 30, 2016 and 2015, the Company incurred $32,000, $0.2 million, $0, $0.1 million, respectively, for these services. The Company's unconsolidated joint ventures incurred $0.1 million, $0.5 million, $0.3 million and $0.7 million, respectively, for these services. Of these costs, $18,000 and $0 was due to TL Fab LP from the Company at September 30, 2016 and December 31, 2015, respectively, and $0.1 million and $0.2 million was due to TL Fab LP from the Company's unconsolidated joint ventures at September 30, 2016 and December 31, 2015, respectively.

The Company may enter into agreements to purchase lots from unconsolidated land development joint ventures of which it is a member. In accordance with ASC 360-20, Property, Plant and Equipment - Real Estate Sales ("ASC 360-20"), the Company will defer its portion of the underlying gain from the joint venture's sale of these lots. When the Company purchases lots directly from the joint venture, the deferred gain is recorded as a reduction to the Company's land basis on the purchased lots. In certain instances, a third party may purchase lots from our unconsolidated joint ventures with the intent to finish the lots. Then, the Company has an option to acquire these finished lots from the third party. In these instances, the Company defers its portion of the underlying gain and records the deferred gain as deferred profit from unconsolidated joint ventures included in accrued expenses and other liabilities in the accompanying condensed consolidated balance sheets. Once the lot is purchased by the Company, the pro-rata share of the previously deferred profit is recorded as a reduction to the Company's land basis in the purchased lots. In both instances, the gain is ultimately recognized when the Company delivers lots to third-party home buyers at the time of future home closing. At September 30, 2016 and December 31, 2015, $0.6 million and $1.2 million, respectively, of deferred gain from lot sale transactions is included in accrued expenses and other liabilities in the accompanying condensed consolidated balance sheets as deferred profit from unconsolidated joint ventures. In addition, at September 30, 2016 and December 31, 2015, $1.4 million and $1.1 million, respectively, of deferred gain from lot sale transactions remained unrecognized and included as a reduction to land basis in the accompanying condensed consolidated balance sheets.

The Company’s land purchase agreement with TNHC-HW Cannery LLC requires profit participation payments due to the joint venture upon the closing of each home. Payment amounts are calculated based upon a percentage of estimated net profits and are due every 90 days after the first home closing. As of September 30, 2016, no new profit

participation was due to TNHC-HW Cannery LLC, and due to a change in estimates, the Company was owed a refund of $0.2 million from TNHC-HW Cannery LLC for profit participation overpayments. Also per the purchase agreement, the Company is due $0.1 million in fee credits from TNHC-HW Cannery LLC at September 30, 2016. Both amounts are included in due from affiliates in the accompanying condensed consolidated balance sheets.
On January 15, 2016, the Company entered into an assignment and assumption of membership interest agreement (the “Buyout Agreement”) for its partner's interest in the TNHC San Juan LLC unconsolidated joint venture. Per the terms of the Buyout Agreement, the Company contributed $20.6 million to the joint venture, and the joint venture made a liquidating cash distribution to our partner for the same amount in exchange for its membership interest. Prior to the buyout, the Company accounted for its investment in TNHC San Juan LLC as an equity method investment. After the buyout, TNHC San Juan LLC is now a wholly owned subsidiary of the Company.
During June 2016, our LR8 Investors LLC unconsolidated joint venture (LR8) made its final distributions, allocated $0.5 million of income to the Company from a reduction in reserves, and our outside equity partner exited the joint venture. Upon

THE NEW HOME COMPANY INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

the change in control, we were required to consolidate this venture as a wholly owned subsidiary, and the Company assumed the cash, accounts receivable, accounts payable, and accrued liabilities, including warranty reserve, of the joint venture. In accordance with ASC 805, Business Combinations, we remeasured the assets and liabilities at fair value at the time of consolidation and recognized a gain of $1.1 million, which is included in equity in net income of unconsolidated joint ventures in the accompanying condensed consolidated statements of operations.

12. Stock-Based Compensation

The 2014 Long-Term Incentive Plan (the “2014 Incentive Plan”), was adopted by our board of directors in January 2014. The 2014 Incentive Plan provides for the grant of equity-based awards, including options to purchase shares of common stock, stock appreciation rights, restricted and unrestricted stock awards, restricted stock units and performance awards. The 2014 Incentive Plan will automatically expire on the tenth anniversary of its effective date. Our board of directors may terminate or amend the 2014 Incentive Plan at any time, subject to any requirement of stockholder approval required by applicable law, rule or regulation and provided that the rights of a holder of an outstanding award may not be impaired without the consent of the holder.

The number of shares of our common stock that are authorized to be issued under the 2014 Incentive Plan is 1,644,875 shares. To the extent that shares of the Company's common stock subject to an outstanding option, stock appreciation right, stock award or performance award granted under the 2014 Incentive Plan or any predecessor plan are not issued or delivered by reason of the expiration, termination, cancellation or forfeiture of such award or the settlement of such award in cash, then such shares of common stock generally shall again be available under the 2014 Incentive Plan.

The Company has issued stock option and restricted stock unit awards under the 2014 Incentive Plan. As of September 30, 2016, 11,484 shares remain available for grant under the 2014 Incentive Plan. The exercise price of stock-based awards may not be less than the market value of the Company's common stock on the date of grant. The fair value for stock options is established at the date of grant using the Black-Scholes model for time-based vesting awards. The Company's stock option and restricted stock awards typically vest over a one to three year period and the stock options expire ten years from the date of grant.

At our 2016 Annual Meeting of Shareholders on May 24, 2016, our shareholders approved the Company's 2016 Incentive Award Plan (the "2016 Incentive Plan"). The 2016 Incentive Plan provides for the grant of stock options, stock appreciation rights, restricted stock, restricted stock units and other stock- or cash-based awards. Non-employee directors of the Company and employees and consultants of the Company or any of its subsidiaries are eligible to receive awards under the 2016 Incentive Plan. The 2016 Incentive Plan authorizes the issuance of 800,000 shares of common stock, subject to certain limitations. The 2016 Incentive Plan may be amended or terminated by the Board at any time, subject to certain limitations requiring stockholder consent or the consent of the participant. The 2016 Incentive Plan will expire on February 23, 2026. At September 30, 2016, no awards had been granted from the 2016 Incentive Plan.

A summary of the Company’s common stock option activity as of and for the nine months ended September 30, 2016 and 2015 is presented below:

	Nine Months Ended September 30,			
	2016		2015	
	Number of Shares	Weighted-Average Exercise Price per Share	Number of Shares	Weighted-Average Exercise Price per Share
Outstanding Stock Option Activity				
Outstanding, beginning of period	840,298	$ 11.00	846,874	$ 11.00

Granted	—	$ —	—	$ —
Exercised	—	$ —	—	$ —
Forfeited	(4,512)	$ 11.00	—	$ —
Outstanding, end of period	835,786	$ 11.00	846,874	$ 11.00
Exercisable, end of period	42,042	$ 11.00	24,717	$ 11.00

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A summary of the Company’s restricted stock unit activity as of and for the nine months ended September 30, 2016 and 2015 is presented below:

	Nine Months Ended September 30,			
	2016		2015	
	Number of Shares	Weighted-Average Grant-Date Fair Value per Share	Number of Shares	Weighted-Average Grant-Date Fair Value per Share
Restricted Stock Unit Activity				
Outstanding, beginning of period	308,386	$ 14.20	112,233	$ 11.36
Granted	414,045	$ 10.05	293,324	$ 14.46
Vested	(231,289)	$ 14.22	(85,386)	$ 11.48
Forfeited	(11,796)	$ 12.10	(384)	$ 11.00
Outstanding, end of period	479,346	$ 10.66	319,787	$ 14.17

The expense related to the Company's stock-based compensation programs, included in general and administrative expense in the accompanying condensed consolidated statements of operations, was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(Dollars in thousands)			
Expense related to:				
Stock options	$300	$301	$747	$911
Restricted stock units	560	941	1,855	1,814
	$860	$1,242	$2,602	$2,725

We used the "simplified method" to establish the expected term of the common stock options granted by the Company. Our restricted stock unit awards are valued based on the closing price of our common stock on the date of grant. At September 30, 2016, the amount of unearned stock-based compensation currently estimated to be expensed through 2019 related to unvested common stock options and restricted stock units is $4.1 million, net of estimated forfeitures. The weighted-average period over which the unearned stock-based compensation is expected to be recognized is 2.0 years. If there are any modifications or cancellations of the underlying unvested awards, the Company may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense.

13. Income Taxes

The Company accounts for income taxes in accordance with ASC 740, which requires an asset and liability approach for measuring deferred taxes based on temporary differences between the financial statements and tax bases of assets and liabilities existing at each balance sheet date using enacted tax rates for the years in which taxes are expected to be paid or recovered.

For the three months ended September 30, 2016 and 2015, the Company recorded a provision for income taxes of $3.5 million and $2.2 million, respectively. The effective tax rate for the three months ended September 30, 2016 and 2015 differs from the 35% federal statutory tax rate due to the tax benefit of production activities, partially offset by state income taxes and return to provision adjustments during the 2015 and 2016 third quarters.

For the nine months ended September 30, 2016 and 2015, the Company recorded a provision for income taxes of $4.7 million and $5.3 million, respectively. Included in the nine month period for 2016 is an allocation of income from LR8 of $0.5 million and a $1.1 million gain from the closeout of our LR8 joint venture, which resulted in a provision for income taxes of $0.6 million for the nine month period ended September 30, 2016 and did not impact our effective tax rate. The effective tax rate for the nine month periods differs from the 35% federal statutory tax rate, primarily due to the tax benefit of production activities, partially offset by state income taxes and return to provision adjustments during the nine months ended September 30, 2016 and 2015 and stock compensation shortfalls in excess of available additional paid-in capital (“APIC”) pools during the nine months ended September 30, 2016.

Each quarter we assess our deferred tax asset to determine whether all or any portion of the asset is more likely than not unrealizable under ASC 740. We are required to establish a valuation allowance for any portion of the asset we conclude is more likely than not unrealizable. Our assessment considers, among other things, the nature, frequency and severity of prior cumulative losses, forecasts of future taxable income, the duration of statutory carryforward periods, our utilization experience with operating loss and tax credit carryforwards and the planning alternatives, to the extent these items are applicable.

The Company classifies any interest and penalties related to income taxes assessed by jurisdiction as part of income tax expense. The Company has concluded that there were no significant uncertain tax positions requiring recognition in its financial statements, nor has the Company been assessed interest or penalties by any major tax jurisdictions related to any open tax periods.

14. Segment Information

The Company’s operations are organized into two reportable segments: homebuilding and fee building. In accordance with ASC 280, in determining the most appropriate reportable segments, we considered similar economic and other characteristics, including product types, gross margins, production processes, suppliers, subcontractors, regulatory environments, land acquisition results, and underlying demand and supply.

The reportable segments follow the same accounting policies as our consolidated financial statements described in Note 1. Operational results of each reportable segment are not necessarily indicative of the results that would have been achieved had the reportable segment been an independent, stand-alone entity during the periods presented.

Financial information relating to reportable segments was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(Dollars in thousands)			
Revenues:				
Homebuilding	$125,142	$57,878	$246,281	$133,315
Fee building, including management fees	52,761	29,099	125,726	102,158
Total	$177,903	$86,977	$372,007	$235,473
Income before income taxes:				
Homebuilding	$7,113	$4,523	$6,207	$8,296
Fee building, including management fees	1,929	2,071	5,663	6,144
Total	$9,042	$6,594	$11,870	$14,440

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	

Assets:		
Homebuilding	$496,065	$331,697
Fee building	20,758	19,573
Total	$516,823	$351,270

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

15. Supplemental Disclosure of Cash Flow Information

The following table presents certain supplemental cash flow information:

	Nine months ended September 30,	
	2016	2015
	(Dollars in thousands)	
Supplemental disclosures of cash flow information		
Interest paid, net of amounts capitalized	$—	$—
Income taxes paid	$8,270	$8,356
Supplemental disclosures of non-cash transactions		
Purchase of real estate with notes payable to affiliate	$—	$747
Contribution of real estate to unconsolidated joint ventures	$—	$18,828
Contribution of real estate from noncontrolling interest in subsidiary	$—	$1,301
Assets assumed from unconsolidated joint ventures	$46,811	$—
Liabilities and equity assumed from unconsolidated joint ventures	$47,197	$—

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

CAUTIONARY NOTE CONCERNING FORWARD-LOOKING STATEMENTS

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act, as amended. All statements contained in this quarterly report on Form 10-Q other than statements of historical fact, including statements regarding our future results of operations and financial position, our business strategy and plans, and our objectives for future operations, are forward-looking statements. These forward-looking statements are frequently accompanied by words such as "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "expect," "goal," "plan" and similar expressions. We have based these forward-looking statements large on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs.

These forward-looking statements are subject to a number of risks, uncertainties, and assumptions, including those described in Part I, Item 1A, "Risk Factors" and Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our annual report on Form 10-K for the year ended December 31, 2015. The following factors, among others, may cause our actual results, performance or achievements to differ materially from any future results, performance or achievements expressed or implied by these forward-looking statements:

- economic changes either nationally or in the markets in which we operate, including declines in employment, volatility of mortgage interest rates and inflation;
- shortages of or increased prices for labor, land or raw materials used in housing construction;
- a downturn in the homebuilding industry;
- volatility and uncertainty in the credit markets and broader financial markets;
- our business and investment strategy;
- availability of land to acquire and our ability to acquire such land on favorable terms or at all;
- our liquidity and availability, terms and deployment of capital;
- delays in land development or home construction resulting from adverse weather conditions, regulatory approval delays, or other events outside our control;
- our customers' ability to obtain mortgage financing;
- issues concerning our joint venture partnerships;
- the cost and availability of insurance and surety bonds;
- changes in, or the failure or inability to comply with, governmental laws and regulations;
- the timing of receipt of regulatory approvals and the opening of projects;
- the degree and nature of our competition;
- our leverage and debt service obligations;
- restrictive covenants relating to our operations in our current or future financing arrangements; and
- availability of qualified personnel and our ability to retain our key personnel.
- the impact of recent accounting standards.

Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the future events and trends discussed in this quarterly report on Form 10-Q may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward-looking statements.

The forward-looking statements in this quarterly report on Form 10-Q speak only as of the date of this quarterly report on Form 10-Q, and we undertake no obligation to revise or publicly release any revision to these forward-looking statements, except as required by law. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

Consolidated Financial Data

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
	(Dollars in thousands)			
Revenues:				
Home sales	$125,142	$57,878	$246,281	$133,315
Fee building, including management fees from unconsolidated joint ventures of $1,539, $3,255, $6,251 and $8,356, respectively	52,761	29,099	125,726	102,158
	177,903	86,977	372,007	235,473
Expenses:				
Cost of homes sales	105,799	48,741	211,859	112,747
Cost of fee building	50,832	27,028	120,063	96,014
Selling and marketing	6,055	3,442	14,577	7,531
General and administrative	6,468	5,105	17,476	13,078
	169,154	84,316	363,975	229,370
Equity in net income of unconsolidated joint ventures	488	4,056	4,428	9,180
Other expense, net	(195)	(123)	(590)	(843)
Income before income taxes	9,042	6,594	11,870	14,440
Provision for income taxes	(3,465)	(2,249)	(4,718)	(5,275)
Net income	5,577	4,345	7,152	9,165
Net (income) loss attributable to noncontrolling interest	(30)	99	90	297
Net income attributable to The New Home Company Inc.	$5,547	$4,444	$7,242	$9,462

Overview

The Company delivered solid top and bottom line growth during the 2016 third quarter, while continuing to lay the foundation for future success by focusing more on its wholly owned operations. We grew our wholly owned community count by 30% year-over-year to 13 actively selling communities, home sales revenue by 116%, and our estimated backlog value by 37% to $290 million. At the same time, we grew our investment in wholly owned real estate inventories by $182.8 million, or 91%, since December 31, 2015 and our wholly owned lots owned and controlled by 20% to nearly 1,600 lots.

Total revenues for the 2016 third quarter were $177.9 million, compared to $87.0 million in the prior year period. Net income attributable to the Company was $5.5 million, or $0.27 per diluted share, compared to net income of $4.4 million, or $0.27 per diluted share, in the prior year period. The year-over-year increase in net income was primarily attributable to a 105% increase in total revenues, a 480 basis point reduction in selling, general and administrative ("SG&A") expenses as a percentage of home sales revenue, which was partially offset by a $3.6 million reduction in joint venture income. The increase in revenues and improvement in our SG&A leverage is consistent with the shift in focus to our wholly owned operations.

Results of Operations

Net New Home Orders

	Three Months Ended September 30,		Increase/(Decrease)		Nine Months Ended September 30,		Increase/(Decrease)	
	2016	2015	Amount	%	2016	2015	Amount	%
	(Dollars in thousands)							
Net new home orders								
Southern California	39	32	7	22 %	105	68	37	54 %
Northern California	25	29	(4)	(14)%	79	58	21	36 %
	64	61	3	5 %	184	126	58	46 %
Selling communities at end of period								
Southern California					8	4	4	100 %
Northern California					5	6	(1)	(17)%
					13	10	3	30 %
Monthly sales absorption rate per community	1.7	2.3	(0.6)	(26)%	1.8	2.1	(0.3)	(14)%
Cancellation rate	11 %	8 %	3 %	N/A	12 %	6 %	6 %	N/A

Net new home orders for the three and nine months ended September 30, 2016 increased 5% and 46%, respectively. The increases as compared to the same periods in 2015 were primarily driven by an increase in the number of average selling communities, which was partially offset by slower monthly sales absorption rates.

Backlog

	As of September 30,								
	2016			2015			% Change		
	Homes	Dollar Value	Average Price	Homes	Dollar Value	Average Price	Homes	Dollar Value	Average Price
	(Dollars in thousands)								
Southern California	92	$262,224	$ 2,850	59	$172,380	$ 2,922	56%	52 %	(2)%
Northern California	37	27,971	756	37	39,260	1,061	—%	(29)%	(29)%
Total	129	$290,195	$ 2,250	96	$211,640	$ 2,205	34%	37 %	2 %

Backlog reflects the number of homes, net of cancellations, for which we have entered into a sales contract with a customer, but for which we have not yet delivered the home. The dollar value of backlog was up 37% to $290.2 million primarily due to a 34% increase in the number of homes in backlog, and to a lesser extent, a 2% increase in the average selling price of homes in backlog to $2.2 million. The higher dollar value in backlog in Southern California as compared to Northern California was due to higher community counts in Southern California combined with higher-priced communities, particularly in Newport Coast where we have three coastal luxury communities where average home prices range from $4 million to $7 million. The increase in number of homes in backlog as of September 30, 2016 compared to the prior year period was the result of increased net new home orders due to an increase in the number of selling communities.

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Lots Owned and Controlled

	September 30,		Increase/(Decrease)	
	2016	2015	Amount	%
Lots Owned				
Southern California	287	135	152	113 %
Northern California	339	292	47	16 %
Total	626	427	199	47 %
Lots Controlled [(1)]				
Southern California	693	569	124	22 %
Northern California	265	80	185	231 %
Total	958	649	309	48 %
Total Lots Owned and Controlled - Wholly Owned	1,584	1,076	508	47 %
Fee Building [(2)]	981	1,498	(517)	(35)%
Total Lots Owned and Controlled	2,565	2,574	(9)	— %

Consistent with our focus to grow our wholly owned business, the Company increased its number of wholly owned lots owned and controlled by 47% year-over-year.

(1) Includes lots that we control under purchase and sale agreements or option agreements subject to customary conditions and have not yet closed. There can be no assurance that such acquisitions will occur.
(2) Subject to agreements with property owners.

Home Sales Revenue and New Homes Delivered

	Three Months Ended September 30,								
	2016			2015			% Change		
	Homes	Dollar Value	Average Price	Homes	Dollar Value	Average Price	Homes	Dollar Value	Average Price
	(Dollars in thousands)								
Southern California	36	$105,789	$2,939	15	$40,354	$2,690	140%	162 %	9 %
Northern California	24	19,353	806	15	17,524	1,168	60 %	10 %	(31)%
Total	60	$125,142	$2,086	30	$57,878	$1,929	100%	116 %	8 %

	Nine Months Ended September 30,								
	2016			2015			% Change		
	Homes	Dollar Value	Average Price	Homes	Dollar Value	Average Price	Homes	Dollar Value	Average Price
	(Dollars in thousands)								
Southern California	67	$189,996	$2,836	42	$106,049	$2,525	60 %	79 %	12 %
Northern California	64	56,285	879	29	27,266	940	121%	106 %	(6)%
Total	131	$246,281	$1,880	71	$133,315	$1,878	85 %	85 %	— %

New home deliveries increased 100% and 85%, respectively, during the three and nine months ended September 30, 2016 compared to the same periods in 2015. The increase in deliveries was the result of a higher number of homes in beginning backlog for each period and an increase in the number of net new home orders generated during the respective periods. For the three and nine months ended September 30, 2016, home sales revenue increased 116% and

85%, respectively, compared to the same periods in 2015, primarily due to an increase in the number of homes delivered, coupled with an 8% higher average sales price for the 2016 third quarter. Southern California is our largest operation and represented 85% and 77% of our home sales revenue for the three and nine month periods ended September 30, 2016. The higher revenues and average home prices in

Southern California as compared to Northern California were driven by higher-priced, luxury coastal communities in top-notch master plans located in Orange County, California. The average selling prices in Northern California as compared to Southern California were lower primarily due to the relative geographic location of the communities in which we currently have deliveries, none of which are coastal, as well as the delivery of smaller attached product.

Homebuilding Gross Margin

Homebuilding gross margin percentage for the three and nine months ended September 30, 2016 was 15.5% and 14.0%, respectively, compared to 15.8% and 15.4%, respectively, for the same periods in 2015. The year-over-year change in gross margin percentages was primarily due to a change in the mix of homes delivered and was partially offset by a 90 basis point benefit from a warranty accrual adjustment made during the 2016 third quarter that increased homebuilding gross margin by $1.1 million. In order to reflect more comparable gross margin and SG&A percentage metrics with other homebuilders, effective January 1, 2016, we started amortizing certain capitalizable selling and marketing costs associated with model set-up to selling and marketing expenses versus through cost of home sales. As a result of this change, we reclassified $1.1 million and $2.6 million, respectively, in capitalizable selling and marketing costs for the three and nine months ended September 30, 2015 out of cost of home sales to selling and marketing expenses to conform with current year presentation.

Excluding interest in cost of home sales, adjusted homebuilding gross margin percentage for the three and nine months ended September 30, 2016 was 16.5% and 15.2%, respectively, compared to 16.5% and 16.1%, respectively, for the same periods in 2015. Adjusted homebuilding gross margin percentage is a non-GAAP financial measure. See the table below reconciling this non-GAAP financial measure to homebuilding gross margin, the nearest GAAP equivalent.

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2016	%	2015	%	2016	%	2015	%
	(Dollars in thousands)							
Home sales revenue	$125,142	100.0%	$57,878	100.0%	$246,281	100.0%	$133,315	100.0%
Cost of home sales	105,799	84.5 %	48,741	84.2 %	211,859	86.0 %	112,747	84.6 %
Homebuilding gross margin	19,343	15.5 %	9,137	15.8 %	34,422	14.0 %	20,568	15.4 %
Add: Interest in cost of home sales	1,306	1.0 %	396	0.7 %	3,017	1.2 %	876	0.7 %
Adjusted homebuilding gross margin[(1)]	$20,649	16.5 %	$9,533	16.5 %	$37,439	15.2 %	$21,444	16.1 %

(1) Adjusted homebuilding gross margin is a non-GAAP financial measure. We believe that by adding interest in cost of home sales back to homebuilding gross margin, investors are able to assess the performance of our homebuilding business excluding our interest cost. We believe this information is meaningful as it isolates the impact that leverage has on homebuilding gross margin and permits investors to make better comparisons with our competitors who adjust gross margins in a similar fashion.

Fee Building

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2016	%	2015	%	2016	%	2015	%
	(Dollars in thousands)							
Fee building revenues	$52,761	100.0%	$29,099	100.0%	$125,726	100.0%	$102,158	100.0%
Cost of fee building	50,832	96.3 %	27,028	92.9 %	120,063	95.5 %	96,014	94.0 %
Fee building gross margin	$1,929	3.7 %	$2,071	7.1 %	$5,663	4.5 %	$6,144	6.0 %

Fee building revenues include (i) billings to independent third-party land owners for general contracting services and (ii) management fees from our unconsolidated joint ventures for construction management services. Cost of fee building includes (i) labor, subcontractor, and other indirect construction and development costs that are reimbursable by the land owner and (ii) general and administrative, or G&A, expenses that are attributable to fee building activities. Besides allocable G&A expenses, there are no other material costs associated with management fees from our unconsolidated joint ventures.

Billings to land owners are a function of construction activity and reimbursable costs are incurred as homes are started. The total billings and reimbursable costs are driven by the pace at which the land owner has us execute its development plan. Management fees from our unconsolidated joint ventures are collected over the project's life and increase as homes and lots are delivered.

For the three and nine months ended September 30, 2016, fee building revenues increased 81% and 23%, respectively, from the prior year periods. Included in fee building revenues for the three months ended periods were (i) $51.2 million and $25.8 million of billings to land owners for 2016 and 2015, respectively, and (ii) $1.5 million and $3.3 million of management fees from our unconsolidated joint ventures for 2016 and 2015, respectively. Included in fee building revenues for the nine months ended periods were (i) $119.5 million and $93.8 million of billings to land owners for 2016 and 2015, respectively, and (ii) $6.3 million and $8.4 million of management fees from our unconsolidated joint ventures for 2016 and 2015, respectively. The overall increase in fee building revenues was primarily driven by an increase in construction activity at our fee building projects and offset partially by a decline in management fees from unconsolidated joint ventures, which was due to a reduction in the number of homes and lots delivered by our joint venture communities.

Our fee building revenues have historically been concentrated with a small number of customers. For the three and nine months ended September 30, 2016 and 2015, one customer comprised 97%, 95%, 88% and 92% of fee building revenue, respectively.

For the three and nine months ended September 30, 2016, cost of fee building increased due to the increase in fee building revenues, compared to the same periods during 2015. The amount of G&A expenses included in cost of fee building was $2.2 million, $6.6 million, $2.4 million and $6.7 million respectively, for the three and nine months ended September 30, 2016 and 2015, respectively. Fee building gross margin percentage decreased to 3.7% from 7.1% for the three months ended September 30, 2016 and decreased to 4.5% from 6.0% for the nine months ended September 30, 2016 as compared to the prior year periods. The overall decrease in gross margin was primarily driven by a decrease in management fees from our unconsolidated joint ventures due to a reduction in the number of homes and lots delivered by our joint venture communities, which was partially offset by a slightly higher fee rate with our largest customer on certain projects.

Selling, General and Administrative Expenses

	Three Months Ended September 30,		As a Percentage of Home Sales Revenue				Nine Months Ended September 30,		As a Percentage of Home Sales Revenue			
	2016	2015	2016		2015		2016	2015	2016		2015	
	(Dollars in thousands)											
Selling and marketing expenses	$6,055	$3,442	4.8	%	5.9	%	$14,577	$7,531	5.9	%	5.6	%
General and administrative expenses (“G&A”)	6,468	5,105	5.2	%	8.8	%	17,476	13,078	7.1	%	9.8	%
Total selling, marketing and G&A (“SG&A”)	$12,523	$8,547	10.0	%	14.8	%	$32,053	$20,609	13.0	%	15.4	%

SG&A expenses for the three and nine months ended September 30, 2016 were up for each year-over-year period consistent with the increase in our wholly owned community count and higher revenue totals. However, our SG&A operating leverage improved significantly due to the increase in home sales revenue, resulting in a 480 basis point reduction in our SG&A expense ratio for the 2016 third quarter and a 240 basis point improvement for the nine month period ended September 30, 2016.

Equity in Net Income of Unconsolidated Joint Ventures

As of September 30, 2016 and 2015, we had ownership interests in 13 unconsolidated joint ventures. We own economic interests in our unconsolidated joint ventures, which include our capital interests that generally range from 5% to 35% plus, in each case, a share of the distributions from the unconsolidated joint ventures in excess of our capital interest if certain minimum returns are achieved. These economic interests vary among our different unconsolidated joint ventures.

Our share of joint venture income decreased for the three months ended September 30, 2016 compared to the same period in 2015 due to a decrease in total revenues of the joint ventures which was driven by fewer new home deliveries and a 43% decrease in the average sales price of homes delivered. Our share of joint venture income also decreased for the nine months ended September 30, 2016 due to a reduction in total joint venture revenues, but was partially offset by a one-time gain related to the close-out of one joint venture. During the second quarter of 2016, the

Company closed out one of its unconsolidated joint ventures known as "LR8" and received an income allocation of $0.5 million from a reserve reduction prior to the close out. As part of this transaction, the Company also recognized a gain of $1.1 million due to the purchase of our JV partner's interest for less than its carrying value.

The following sets forth supplemental operational and financial information about our unconsolidated joint ventures. Such information is not included in our financial data for GAAP purposes, but is recognized in our results as a component of equity in net income of unconsolidated joint ventures. This data is included for informational purposes only.

	Three Months Ended September 30,		Increase/(Decrease)		Nine Months Ended September 30,		Increase/(Decrease)	
	2016	2015	Amount	%	2016	2015	Amount	%
	(Dollars in thousands)							
Unconsolidated Joint Ventures—Homebuilding Operational Data								
Net new home orders	35	57	(22)	(39)%	111	268	(157)	(59)%
Monthly sales absorption rate per community	2.5	1.8	0.7	39 %	2.5	3.1	(0.6)	(19)%
Cancellation rate	15 %	15 %	— %	N/A	12 %	8 %	4 %	N/A
New homes delivered	23	71	(48)	(68)%	123	170	(47)	(28)%
Home sales revenue	$19,659	$106,485	$(86,826)	(82)%	$105,558	$200,325	$(94,767)	(47)%
Average sales price of homes delivered	$855	$1,500	$(645)	(43)%	$858	$1,178	$(320)	(27)%
Selling communities at end of period					8	11	(3)	(27)%
Backlog (dollar value)					$85,317	$205,604	$(120,287)	(59)%
Backlog (homes)					88	173	(85)	(49)%
Average sales price of backlog					$970	$1,188	$(218)	(18)%

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2016	%	2015	%	2016	%	2015	%
	(Dollars in thousands)							
Unconsolidated Joint Ventures—Homebuilding Gross Margin								
Unconsolidated joint ventures home sales revenue	$19,659	100.0%	106,485	100.0%	$105,558	100.0%	$200,325	100.0%
Cost of unconsolidated joint ventures home sales	14,498	73.7 %	80,077	75.2 %	79,659	75.5 %	155,528	77.6 %
Unconsolidated joint ventures homebuilding gross margin	5,161	26.3 %	26,408	24.8 %	25,899	24.5 %	44,797	22.4 %
Add: Interest in cost of unconsolidated joint venture home sales	287	1.4 %	1,091	1.0 %	1,499	1.5 %	2,654	1.3 %
Adjusted unconsolidated joint ventures homebuilding gross margin [1]	$5,448	27.7 %	$27,499	25.8 %	$27,398	26.0 %	$47,451	23.7 %

(1) Adjusted unconsolidated joint ventures homebuilding gross margin is a non-GAAP financial measure. We believe that by adding interest in cost of unconsolidated joint venture home sales back to unconsolidated joint ventures homebuilding gross margin, investors are able to assess the performance of our unconsolidated joint ventures excluding interest cost. We believe this information is meaningful as it isolates the impact that leverage has on unconsolidated joint venture homebuilding gross margin and permits investors to make better comparisons with our competitors who adjust gross margins in a similar fashion.

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	Three Months Ended September 30, 2016	2015	Increase/(Decrease) Amount	%	Nine Months Ended September 30, 2016	2015	Increase/(Decrease) Amount	%
	(Dollars in thousands)							
Unconsolidated Joint Ventures—Land Operational Data								
Land sales revenue	$14,805	$8,885	$ 5,920	67 %	$40,967	$54,455	$(13,488)	(25)%
Backlog (dollar value)(1)					$5,416	$51,662	$(46,246)	(90)%

(1) Amounts include $0 and $18.1 million of backlog dollar value related to purchase contracts between an unconsolidated joint venture and the Company as of September 30, 2016 and 2015, respectively.

	September 30, 2016	2015	Increase/(Decrease) Amount	%
Unconsolidated Joint Ventures—Lots Owned and Controlled				
Homebuilding				
Lots owned	589	776	(187)	(24)%
Lots controlled (1)	72	68	4	6 %
Homebuilding Total	661	844	(183)	(22)%
Land Development				
Lots owned	2,180	2,420	(240)	(10)%
Lots controlled (1)	235	235	—	— %
Land Development Total	2,415	2,655	(240)	(9)%
Total	3,076	3,499	(423)	(12)%

(1) Consists of lots that are under purchase and sale agreements.

Provision (Benefit) for Income Taxes

For the three months ended September 30, 2016 and 2015, the Company recorded a provision for income taxes of $3.5 million and $2.2 million, respectively. The effective tax rate for the three months ended September 30, 2016 and 2015 differs from the 35% federal statutory tax rate due to the tax benefit of production activities, partially offset by state income taxes and return to provision adjustments during the 2015 and 2016 third quarters.

For the nine months ended September 30, 2016 and 2015, the Company recorded a provision for income taxes of $4.7 million and $5.3 million, respectively. Included in the nine month period for 2016 is an allocation of income of $0.5 million from LR8 and a $1.1 million gain from the closeout of our LR8 joint venture, which resulted in a provision for income taxes of $0.6 million for the nine month period ended September 30, 2016 and did not impact our effective tax rate. The effective tax rate for the nine month periods differs from the 35% federal statutory tax rate, primarily due to the tax benefit of production activities, partially offset by state income taxes and return to provision adjustments during the nine months ended September 30, 2016 and 2015 and stock compensation shortfalls in excess of available additional paid-in capital (“APIC”) pools during the nine months ended September 30, 2016.

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Liquidity and Capital Resources

Overview

Our principal uses of capital for the nine months ended September 30, 2016 were land purchases, land development, home construction, contributions to our unconsolidated joint ventures, operating expenses, repayments on our credit facility and the payment of routine liabilities. Our principal sources of capital for the nine months ended September 30, 2016 were advances from our senior unsecured revolving credit facility, cash generated from home sales activities and distributions from our unconsolidated joint ventures.

Cash flows for each of our communities depend on their stage in the development cycle, and can differ substantially from reported earnings. Early stages of development or expansion require significant cash outlays for land acquisitions, entitlements and other approvals, and construction of model homes, roads, utilities, general landscaping and other amenities. Because these costs are a component of our real estate inventories and not recognized in our consolidated statement of operations until a home is delivered, we incur significant cash outlays prior to our recognition of earnings. In the later stages of community development, cash inflows may significantly exceed earnings reported for financial statement purposes, as the cash outflow associated with home and land construction was previously incurred. From a liquidity standpoint, we are actively acquiring and developing lots to increase our lot supply and community count. As we continue to expand our business, we expect cash outlays for land purchases, land development and home construction to exceed our cash generated by operations.

We exercise strict controls and believe we have a prudent strategy for companywide cash management, including those related to cash outlays for land and inventory acquisition, development and investments in unconsolidated joint ventures. We ended the third quarter of 2016 with $44.3 million of cash and cash equivalents, a $1.6 million decrease from December 31, 2015, primarily as a result of net increased investment in real estate inventories of $159.8 million, partially offset by net borrowings of $139.7 million due to the growth in community count and operations. We expect to generate cash from the sale of our inventory, but intend to redeploy the net cash generated from the sale of inventory to acquire and develop strategic, well-positioned lots that represent opportunities to generate future income and cash flows.

As of September 30, 2016 and December 31, 2015, we had $17.9 million and $16.7 million, respectively, in accounts payable that related to costs incurred under our fee building agreements. Funding to pay these amounts is the obligation of the independent third-party land owner, which is generally funded on a monthly basis. Similarly, contracts and accounts receivable as of the same dates included $19.5 million and $17.8 million, respectively, related to the payment of the above payables.

We intend to utilize both debt and equity as part of our ongoing financing strategy, coupled with redeployment of cash flows from continuing operations, to provide us with the financial flexibility to operate our business. In that regard, we expect to employ prudent levels of leverage to finance the acquisition and development of our lots and construction of our homes. As of September 30, 2016, we had outstanding borrowings of $233.9 million. We will consider a number of factors when evaluating our level of indebtedness and when making decisions regarding the incurrence of new indebtedness, including the purchase price of assets to be acquired with debt financing, the estimated market value of our assets and the ability of particular assets, and our company as a whole, to generate cash flow to cover the expected debt service. In addition, our senior unsecured revolving credit facility contains certain financial covenants that limits the amount of leverage we can maintain.

We intend to finance future acquisitions and developments with what we believe to be the most advantageous source of capital available to us at the time of the transaction, which may include a combination of secured and unsecured corporate level debt, property-level debt and mortgage financing, other public, private or bank debt, or common and preferred equity. Additionally, we have an existing effective shelf registration statement that allows us to issue equity, debt or hybrid securities up to $349.7 million as of September 30, 2016.

Land Acquisition Notes

The Company has a term loan with a land seller, secured by real estate, which bears interest at 7.0% per annum. As of September 30, 2016, the total available commitment under the note is $4.0 million, all of which has been funded. The note matures on the earlier of (i) 10 days following entitlement approval, or (ii) December 15, 2016. Interest is payable monthly and the remaining principal is due at maturity.

Senior Unsecured Revolving Credit Facility

We have a senior unsecured revolving credit facility (the “Credit Facility”) with a bank group. In May 2016, we increased the commitment under the Credit Facility from $200 million to $260 million with an accordion feature that allows borrowings thereunder to be increased up to an aggregate of $350 million and extended the maturity date by one year to April 30, 2019. As of September 30, 2016, we had $229.9 million outstanding under the credit facility and $30.1 million in availability. We may repay advances at any time without premium or penalty. Interest is payable monthly and is charged at a rate of 1-month LIBOR plus a margin ranging from 2.25% to 3.00% depending on the Company’s leverage ratio as calculated at the end of each fiscal quarter. As of September 30, 2016, the interest rate under the Credit Facility was 3.28%.

Under our Credit Facility, we are required to comply with certain financial covenants, including but not limited to those summarized in the table below, and as described and defined further in the Credit Facility:

Financial Covenants	Actual at September 30, 2016	Covenant Requirement at September 30, 2016
	(Dollars in thousands)	
Unencumbered Liquid Assets	$44,254	$ 7,000
EBITDA to Interest Incurred	5.7 : 1.0	> 1.5 : 1.0
Tangible Net Worth	$229,875	$ 169,028
Leverage Ratio	46 %	< 65%
Adjusted Leverage Ratio (1)	44 %	< 50%

(1) Adjusted Leverage Ratio is computed as total joint venture debt divided by total joint venture equity.

We were in compliance with all financial covenants as of September 30, 2016.

Debt-to-Capital Ratios

We believe that debt-to-capital ratios provide useful information to the users of our financial statements regarding our financial position and leverage. Net debt-to-capital ratio is a non-GAAP financial measure. See the table below reconciling this non-GAAP measure to debt-to-capital ratio, the nearest GAAP equivalent. The ratio of debt-to-capital and the ratio of net debt-to-capital are calculated as follows:

	September 30, 2016	December 31, 2015
	(Dollars in thousands)	
Notes payable, including unsecured revolving credit facility	$233,924	$83,082
Equity, exclusive of noncontrolling interest	229,875	220,775
Total capital	$463,799	$303,857
Ratio of debt-to-capital (1)	50.4 %	27.3 %
Notes payable, including unsecured revolving credit facility	$233,924	$83,082
Less: cash, cash equivalents and restricted cash	45,224	46,254
Net debt	188,700	36,828
Equity, exclusive of noncontrolling interest	229,875	220,775
Total capital	$418,575	$257,603
Ratio of net debt-to-capital (2)	45.1 %	14.3 %

(1) The ratio of debt-to-capital is computed as the quotient obtained by dividing notes payable by the sum of total notes payable (including unsecured revolving credit facility) plus equity, exclusive of noncontrolling interest.

(2) The ratio of net debt-to-capital is computed as the quotient obtained by dividing net debt (which is notes payable (including unsecured revolving credit facility) less cash to the extent necessary to reduce the debt balance to zero) by total capital, exclusive of noncontrolling interest. The most directly comparable GAAP financial measure is the ratio of debt-to-capital. We believe the ratio of net debt-to-capital is a relevant financial measure for investors to understand the leverage employed in our operations and as an indicator of our ability to obtain financing. We believe that by deducting our cash from our notes payable, we provide a measure of our indebtedness that takes into account our cash liquidity. We believe this provides useful information as the ratio of debt-to-capital does not

take into account our liquidity and we believe that the ratio net of cash provides supplemental information by which our financial position may be considered. Investors may also find this to be helpful when comparing our leverage to the leverage of our competitors that present similar information. See the table above reconciling this non-GAAP financial measure to the ratio of debt-to-capital.

Cash Flows — Nine Months Ended September 30, 2016 Compared to Nine Months Ended September 30, 2015

For the nine months ended September 30, 2016 as compared to the nine months ended September 30, 2015, the comparison of cash flows is as follows:

- Net cash used in operating activities was $146.7 million for the nine months ended September 30, 2016 versus $83.0 million for the nine months ended September 30, 2015. The year-over-year change was primarily a result of a net increase in cash outflows for real estate inventories of $159.8 million in the 2016 period compared to $100.8 million in the 2015 period. The significant investment in real estate inventories in the 2016 period was the result of growth in our community count, increased land spend, and increased construction activity at our wholly owned communities.
- Net cash provided by investing activities was $7.9 million for the nine months ended September 30, 2016 compared to $17.4 million for the nine months ended September 30, 2015. For the nine months ended September 30, 2016, our net distributions from unconsolidated joint ventures (excluding distributions of earnings) were $6.3 million compared to $17.7 million during the nine months ended September 30, 2015 and was the primary reason net cash provided by investing activities decreased. The reduction in distributions from unconsolidated joint ventures primarily related to the reduction in revenues, new home deliveries, and the completion of certain joint venture communities.
- Net cash provided by financing activities was $137.2 million for the nine months ended September 30, 2016 versus $56.9 million for the nine months ended September 30, 2015. The change was primarily driven by net borrowings under our revolving credit facility of $155.0 million in the 2016 period due to the growth in our community count, increased land spend and construction activity at our wholly owned communities versus $57.9 million in the 2015 period.

Off-Balance Sheet Arrangements and Contractual Obligations

Option Contracts

In the ordinary course of business, we enter into land option contracts in order to procure lots for the construction of our homes. We are subject to customary obligations associated with entering into contracts for the purchase of land and improved lots. These purchase contracts typically require a cash deposit and the purchase of properties under these contracts is generally contingent upon satisfaction of certain requirements by the sellers, including obtaining applicable property and development entitlements. We also utilize option contracts with land sellers as a method of acquiring land in staged takedowns, to help us manage the financial and market risk associated with land holdings, to reduce the use of funds from our corporate financing sources, and to enhance our return on equity. Option contracts generally require a non-refundable deposit for the right to acquire lots over a specified period of time at pre-determined prices. We generally have the right at our discretion to terminate our obligations under both purchase contracts and option contracts by forfeiting our cash deposit with no further financial responsibility to the land seller. In some instances, we may also expend funds for due diligence and development activities with respect to our option contracts prior to purchase which we would have to write off should we not purchase the land. As of September 30, 2016, we had $35.1 million of non-refundable cash deposits pertaining to land option contracts and purchase contracts with an estimated aggregate remaining purchase price of $462.3 million (net of deposits).

Our utilization of land option contracts is dependent on, among other things, the availability of land sellers willing to enter into option arrangements, the availability of capital to financial intermediaries to finance the development of optioned lots, general housing market conditions, and local market dynamics. Options may be more difficult to procure from land sellers in strong housing markets and are more prevalent in certain geographic regions.

Joint Ventures

We enter into land development and homebuilding joint ventures from time to time as means of:

- leveraging our capital base
- accessing larger or highly desirable lot positions
- expanding our market opportunities
- managing financial and market risk associated with land holdings
- establishing strategic alliances

These joint ventures have historically obtained secured acquisition, development and/or construction financing which reduces the use of funds from our corporate financing sources.

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We have provided credit enhancements in connection with joint venture borrowings in the form of loan-to-value ("LTV") maintenance agreements in order to secure the joint venture's performance under the loans and maintenance of certain LTV ratios. We have also entered into agreements with our partners in each of the unconsolidated joint ventures whereby we and our partners are apportioned liability under the LTV maintenance agreements according to their respective capital interest. In addition, the agreements provide us, to the extent our partner has an unpaid liability under such credit enhancements, the right to receive distributions from the unconsolidated joint venture that would otherwise be made to the partner. However, there is no guarantee that such distributions will be made or will be sufficient to cover the share of the liability apportioned to us. The loans underlying the LTV maintenance agreements comprise acquisition and development loans, construction revolvers and model home loans, and the agreements remain in force until the loans are satisfied. Due to the nature of the loans, the outstanding balance at any given time is subject to a number of factors including the status of site improvements, the mix of horizontal and vertical development underway, the timing of phase build outs, and the period necessary to complete the escrow process for homebuyers. As of September 30, 2016 and December 31, 2015, $81.7 million and $74.1 million, respectively, was outstanding under the loans and credit enhanced by us through LTV maintenance agreements. Under the terms of the joint venture agreements, our proportionate share of LTV maintenance agreement liabilities was $12.0 million and $22.5 million as of September 30, 2016 and December 31, 2015, respectively. In addition, we have provided completion guaranties regarding specific performance for certain projects whereby we are required to complete the given project with funds provided by the beneficiary of the guaranty. If there are not adequate funds available under the specific project loans, then we would be subject to financial liability under such completion guaranties. Typically, under such terms of our joint venture agreements, we have the right to apportion the respective share of any liabilities funded under such completion guaranties to our partners. However, there is no guarantee that we will be able to recover against our partners for such amounts owed to us under the terms of such joint venture agreements.

As of September 30, 2016, we held membership interests in 13 unconsolidated joint ventures, nine of which related to homebuilding activities and four of which related to land development as noted below. We were a party to four LTV maintenance agreements related to unconsolidated joint ventures as of September 30, 2016. The following table reflects certain financial and other information related to our unconsolidated joint ventures as of September 30, 2016 :

Joint Venture (Project Name)	Year Formed	Location	Ownership %	As of September 30, 2016 Total Joint Venture Assets	Debt[1]	Equity	Debt-to-Total Capitalization		Loan-to-Value Maintenance Agreement	Future Capital Commitment[2]
				(Dollars in 000's)						
Larkspur Land 8 Investors, LLC (Rose Lane)	2011	Larkspur, CA	10%	$2,134	—	$1,149	—	%	N/A	—
TNHC-HW San Jose LLC (Orchard Park)	2012	San Jose, CA	15%	35,310	8,517	24,188	26	%	Yes	—
TNHC-TCN Santa Clarita LP (Villa Metro)[3]	2012	Santa Clarita, CA	10%	2,058	—	787	—	%	N/A	—
TNHC Newport LLC (Meridian)[3]	2013	Newport Beach, CA	12%	4,787	—	2,076	—	%	N/A	—
Encore McKinley Village LLC (McKinley Village)	2013	Sacramento, CA	10%	79,172	12,825	57,008	18	%	Yes	4,000
TNHC Russell Ranch LLC (Russell Ranch)[3][4][5]	2013	Folsom, CA	35%	47,621	20,000	27,331	42	%	No	8,620
TNHC-HW Foster City LLC (Foster Square)[5]	2013	Foster City, CA	35%	10,373	—	2,253	—	%	N/A	—
Calabasas Village LP (Avanti)[3]	2013	Calabasas, CA	10%	61,827	26,016	31,363	45	%	Yes	1,530
TNHC-HW Cannery LLC (Cannery Park)[5]	2013	Davis, CA	35%	18,358	—	9,342	—	%	N/A	—
Arantine Hills Holdings LP (Bedford Ranch)[3][5]	2014	Corona, CA	5%	95,182	—	94,694	—	%	N/A	1,016
TNHC Tidelands LLC (Tidelands)	2015	San Mateo, CA	20%	58,049	34,300	20,526	63	%	Yes	—
TNHC Mountain Shadows LLC (Mountain Shadows)	2015	Paradise Valley, AZ	25%	50,802	27,060	22,907	54	%	No	1,475
DMB/TNHC LLC (Sterling at Silverleaf)	2016	Scottsdale, AZ	50%	561	—	561	—	%	N/A	375
Total Unconsolidated Joint Ventures				$466,234	$128,718	$294,185	30	%		$ 17,016

(1) Scheduled maturities of the unconsolidated joint venture debt as of September 30, 2016 are as follows: no maturities in 2016, $112.3 million matures in 2017, $9.9 matures in 2018 and $6.5 million matures in 2019.
(2) Estimated future capital commitment represents our proportionate share of estimated future contributions as of September 30, 2016. Actual contributions may differ materially.
(3) Certain members of the Company's board of directors are affiliated with entities that have an investment in these joint ventures.
(4) The debt associated with this joint venture consists of a land seller note.
(5) Land development joint ventures.

As of September 30, 2016, the unconsolidated joint ventures were in compliance with their respective loan covenants, where applicable, and we were not required to make any LTV maintenance-related payments during the three and nine months ended September 30, 2016.

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Seasonality

Historically, the homebuilding industry experiences seasonal fluctuations in quarterly operating results and capital requirements. We typically experience the highest new home order activity in spring and summer, although this activity is also highly dependent on the number of active selling communities, timing of new community openings and other market factors. Since it typically takes five to nine months to construct a new home, we deliver more homes in the second half of the year as spring and summer home orders convert to home deliveries. Because of this seasonality, home starts, construction costs and related cash outflows have historically been highest in the second and third quarters, and a higher level of cash receipts from home deliveries occurs during the second half of the year. We expect this seasonal pattern to continue over the long-term, although it may be affected by volatility in the homebuilding industry.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting policies generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Management evaluates such estimates and judgments on an on-going basis and makes adjustments as deemed necessary. Actual results could differ from these estimates if conditions are significantly different in the future.

Our critical accounting estimates and policies have not changed from those reported in Management’s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2015.

Recently Issued Accounting Standards

Note 1 to the accompanying notes to unaudited condensed consolidated financial statements included in this quarterly report on Form 10-Q is incorporated herein by reference.

JOBS Act

We qualify as an "emerging growth company" pursuant to the provisions of the JOBS Act. For as long as we are an "emerging growth company," we may elect certain exemptions from various reporting requirements that are applicable to other public companies that are not "emerging growth companies," including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our annual reports and proxy statements, and exemptions from the requirements of holding shareholder advisory "say-on-pay" votes on executive compensation.

In addition, Section 107 of the JOBS Act also provides that an "emerging growth company" can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. An "emerging growth company" can therefore delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. However, we have chosen to "opt out" of such extended transition period and, as a result, we will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies. Section 107 of the JOBS Act provides that our decision to opt out of the extended transition period for complying with new or revised accounting standards is irrevocable.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk
Information about our market risk is disclosed in Part II, Item 7A, of our Annual Report on Form 10-K for the fiscal year ended December 31, 2015, and is incorporated herein by reference. There have been no material changes during the nine months ended September 30, 2016, to such information.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and is communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Our disclosure controls and procedures are designed to provide a reasonable level of assurance of reaching our desired disclosure control objectives. In designing controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, will be detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error and mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of controls.

At the end of the period being reported upon, we carried out an evaluation, under the supervision and with the participation of our 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 at the reasonable assurance level as of September 30, 2016.

Change in Internal Controls

There was no change in the Company’s internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

We are involved in various claims and litigation arising in the ordinary course of business. We do not believe that any such claims and litigation will materially affect our results of operations or financial position. For more information regarding how we account for legal proceedings, see Note 10, “Commitments and Contingencies,” to our consolidated financial statements included elsewhere in this report, which is incorporated herein by reference.

Item 1A. Risk Factors

There have been no material changes to the risk factors disclosed under Part I, Item 1A “Risk Factors” in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015.

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

None.

Purchases of Equity Securities by the Issuer

The Company did not make any purchases of its common stock during the three months ended September 30, 2016.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

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Item 6. Exhibits

Exhibit Number	Exhibit Description
3.1	Amended and Restated Certificate of Incorporation of The New Home Company Inc. (incorporated by reference to Exhibit 3.1 of the Company's Annual Report on Form 10-K for the year ended December 31, 2013)
3.2	State of Delaware Certificate of Change of Registered Agent and/or Registered Office (incorporated by reference to Exhibit 3.1 of the Company's Current Report on From 8-K filed on August 1, 2016)
3.3	Bylaws of The New Home Company Inc. (incorporated by reference to Exhibit 3.2 of the Company's Current Report on Form 8-K filed on August 1, 2016)
4.1	Specimen Common Stock Certificate of The New Home Company Inc. (incorporated by reference to Exhibit 4.1 of the Company’s Registration Statement on Form S-1 (Amendment No. 10, filed on January 24, 2014))
4.2	Investor Rights Agreement among The New Home Company Inc., TNHC Partners LLC, IHP Capital Partners VI, LLC, WATT/TNHC LLC, TCN/TNHC LP and collectively H. Lawrence Webb, Wayne J. Stelmar, Joseph D. Davis and Thomas Redwitz (incorporated by reference to Exhibit 4.2 of the Company's Annual Report on Form 10-K for the year ended December 31, 2013)
31.1*	Chief Executive Officer Section 302 Certification of the Sarbanes-Oxley Act of 2002
31.2*	Chief Financial Officer Section 302 Certification of the Sarbanes-Oxley Act of 2002
32.1**	Chief Executive Officer Section 906 Certification of the Sarbanes-Oxley Act of 2002
32.2**	Chief Financial Officer Section 906 Certification of the Sarbanes-Oxley Act of 2002
101 *	The following materials from The New Home Company Inc.’s Quarterly Report on Form 10-Q for the quarter ended September 30, 2016, formatted in eXtensible Business Reporting Language (XBRL): (i) Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Operations, (iii) Condensed Consolidated Statement of Equity, (iv) Condensed Consolidated Statements of Cash Flows, and (v) Notes to Unaudited Condensed Consolidated Financial Statements.

* Filed herewith
** Furnished and not filed herewith for purposes of Section 18 of the Securities Exchange Act of 1934, as amended

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.

The New Home Company
Inc.

By: /s/ H. Lawrence Webb
H. Lawrence Webb
Chief Executive Officer

By: /s/ John M. Stephens
John M. Stephens
Chief Financial Officer

Date: November 4, 2016

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