

BOTTOMLINE TECHNOLOGIES INC /DE/

Form 10-Q

November 08, 2016

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended September 30, 2016**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file number: 0-25259**

**Bottomline Technologies (de), Inc.**

**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or other jurisdiction of**  
**incorporation or organization)**

**02-0433294**  
**(I.R.S. Employer**  
**Identification No.)**

**325 Corporate Drive**

**Portsmouth, New Hampshire**  
**(Address of principal executive offices)**

**03801-6808**  
**(Zip Code)**

**(603) 436-0700**

**(Registrant's telephone number, including area code)**

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer (Do not check if a smaller reporting company)

Smaller Reporting Company

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

The number of shares outstanding of the registrant's common stock as of October 31, 2016 was 40,529,993.

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**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****Bottomline Technologies (de), Inc.****Unaudited Condensed Consolidated Balance Sheets****(in thousands)**

	<b>September 30, 2016</b>	<b>June 30, 2016</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 98,706	\$ 97,174
Marketable securities	29,182	35,209
Accounts receivable net of allowances for doubtful accounts of \$960 at September 30, 2016 and \$982 at June 30, 2016	52,689	61,773
Deferred tax assets		6,244
Prepaid expenses and other current assets	17,130	16,141
Total current assets	197,707	216,541
Property and equipment, net	53,718	51,029
Goodwill	201,489	202,028
Intangible assets, net	158,981	164,930
Other assets	16,538	16,682
Total assets	\$ 628,433	\$ 651,210
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 9,313	\$ 10,218
Accrued expenses	26,311	27,512
Deferred revenue	63,616	74,332
Total current liabilities	99,240	112,062
Convertible senior notes	173,229	169,857
Deferred revenue, non-current	19,231	19,086
Deferred income taxes	21,276	28,147
Other liabilities	27,710	27,271
Total liabilities	340,686	356,423
Stockholders equity		
Preferred Stock, \$.001 par value:		
Authorized shares-4,000; issued and outstanding shares-none		
Common Stock, \$.001 par value:		

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Authorized shares-100,000; issued shares- 41,906 at September 30, 2016 and 41,602 at June 30, 2016; outstanding shares-37,926 at September 30, 2016 and 37,770 at June 30, 2016	42	42
Additional paid-in-capital	600,022	591,800
Accumulated other comprehensive loss	(38,767)	(37,668)
Treasury stock: 3,980 shares at September 30, 2016 and 3,832 shares at June 30, 2016, at cost	(79,487)	(75,832)
Accumulated deficit	(194,063)	(183,555)
Total stockholders' equity	287,747	294,787
Total liabilities and stockholders' equity	\$ 628,433	\$ 651,210

See accompanying notes.

**Table of Contents****Bottomline Technologies (de), Inc.****Unaudited Condensed Consolidated Statements of Comprehensive Loss****(in thousands, except per share amounts)**

	<b>Three Months Ended September 30,</b>	
	<b>2016</b>	<b>2015</b>
<b>Revenues:</b>		
Subscriptions and transactions	\$ 52,132	\$ 46,197
Software licenses	2,121	4,115
Service and maintenance	27,673	30,784
Other	1,158	1,785
<b>Total revenues</b>	<b>83,084</b>	<b>82,881</b>
<b>Cost of revenues:</b>		
Subscriptions and transactions	23,886	20,734
Software licenses	128	288
Service and maintenance	13,285	12,978
Other	878	1,335
<b>Total cost of revenues</b>	<b>38,177</b>	<b>35,335</b>
<b>Gross profit</b>	<b>44,907</b>	<b>47,546</b>
<b>Operating expenses:</b>		
Sales and marketing	18,875	20,155
Product development and engineering	12,935	11,260
General and administrative	12,704	8,823
Amortization of intangible assets	6,285	7,279
<b>Total operating expenses</b>	<b>50,799</b>	<b>47,517</b>
(Loss) income from operations	(5,892)	29
Other expense, net	(3,935)	(3,671)
<b>Loss before income taxes</b>	<b>(9,827)</b>	<b>(3,642)</b>
Income tax provision	681	611
<b>Net loss</b>	<b>\$ (10,508)</b>	<b>\$ (4,253)</b>
<b>Basic and diluted net loss per share:</b>	<b>\$ (0.28)</b>	<b>\$ (0.11)</b>

Shares used in computing basic and diluted net loss per share:	37,940	38,004
<b>Other comprehensive loss, net of tax:</b>		
Unrealized (loss) gain on available for sale securities	(57)	8
Minimum pension liability adjustments	15	116
Foreign currency translation adjustments	(1,057)	(6,585)
<b>Other comprehensive loss, net of tax:</b>	<b>(1,099)</b>	<b>(6,461)</b>
Comprehensive loss	\$ (11,607)	\$ (10,714)

See accompanying notes.

**Table of Contents****Bottomline Technologies (de), Inc.****Unaudited Condensed Consolidated Statements of Cash Flows****(in thousands)**

	<b>Three Months Ended</b>	
	<b>September 30,</b>	
	<b>2016</b>	<b>2015</b>
	<b>(in thousands)</b>	
<b>Operating activities:</b>		
Net loss	\$ (10,508)	\$ (4,253)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Amortization of acquired intangible assets	6,285	7,279
Stock compensation expense	8,199	7,588
Depreciation and amortization	4,087	3,077
Deferred income tax benefit	(548)	(822)
Provision for allowances on accounts receivable		161
Excess tax benefits associated with stock compensation	(40)	(27)
Amortization of debt issuance costs	296	296
Amortization of debt discount	3,076	2,865
Amortization of premium on investments	91	68
Write down of fixed assets		17
(Gain) loss on foreign exchange	(192)	130
Changes in operating assets and liabilities:		
Accounts receivable	8,838	3,390
Prepaid expenses and other current assets	(1,052)	(137)
Other assets	127	(1,123)
Accounts payable	(973)	(592)
Accrued expenses	617	(1,026)
Deferred revenue	(10,253)	(5,625)
Other liabilities	447	(340)
<b>Net cash provided by operating activities</b>	<b>8,497</b>	<b>10,926</b>
<b>Investing activities:</b>		
Purchases of held-to-maturity securities		(44)
Proceeds from sales of held-to-maturity securities		44
Purchase of available-for-sale securities	(7,579)	(4,790)
Proceeds from sales of available-for-sale securities	13,460	3,790
Capital expenditures, including capitalization of software costs	(9,909)	(5,830)
<b>Net cash used in investing activities</b>	<b>(4,028)</b>	<b>(6,830)</b>
<b>Financing activities:</b>		
Repurchase of common stock	(3,773)	(21,354)
Proceeds from exercise of stock options and employee stock purchase plan	1,353	1,435
Excess tax benefits associated with stock compensation	40	27



Net cash used in financing activities	(2,380)	(19,892)
Effect of exchange rate changes on cash	(557)	(1,230)
Increase (decrease) in cash and cash equivalents	1,532	(17,026)
Cash and cash equivalents at beginning of period	97,174	121,163
Cash and cash equivalents at end of period	\$ 98,706	\$ 104,137

See accompanying notes.

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**Bottomline Technologies (de), Inc.**

**Notes to Unaudited Condensed Consolidated Financial Statements**

**September 30, 2016**

**Note 1 Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals and adjustments) considered necessary for a fair presentation of the interim financial information have been included. Operating results for the three months ended September 30, 2016, are not necessarily indicative of the results that may be expected for any other interim period or for the fiscal year ending June 30, 2017 (fiscal year 2017). For further information, refer to the financial statements and footnotes included in the Annual Report on Form 10-K as filed with the Securities and Exchange Commission (SEC) on August 29, 2016.

**Note 2 Recent Accounting Pronouncements**

*Recently Adopted Pronouncements*

In June 2014, the Financial Accounting Standards Board (FASB) issued an accounting standard update which eliminated the definition of a development stage entity and the financial reporting requirements specific to development stage entities. The update also eliminated an exception that previously existed in the consolidation accounting standard for determining whether a development stage entity had sufficient equity at risk and therefore was a variable interest entity (VIE). We adopted this standard effective July 1, 2016. Upon adoption, we were required to re-assess whether one of the entities in which we have an equity investment is a VIE. Based on the re-assessment, we concluded that this entity is a VIE, but that we are not the primary beneficiary (the primary beneficiary of a VIE is required to consolidate the VIE). Accordingly, the adoption of this standard did not have a material impact on our financial statements.

In August 2014, the FASB issued an accounting standard update which requires management to evaluate, at each annual or interim reporting period, whether there are conditions or events that exist that raise substantial doubt about an entity's ability to continue as a going concern within one year after the date the financial statements are issued and provide related disclosures. We adopted this standard on July 1, 2016. The adoption of this standard did not have a material impact on our financial statements.

In April 2015, the FASB issued an accounting standard update which requires that debt issuance costs be presented in the balance sheet as a direct reduction to the carrying value of the debt. We retrospectively adopted this standard effective July 1, 2016 and reclassified debt issuance costs from non-current assets to convertible senior notes in our consolidated balance sheets in all periods presented. Deferred debt issuance costs were approximately \$1.4 million at September 30, 2016 and \$1.7 million at June 30, 2016.

In April 2015, the FASB issued an accounting standard update which provides guidance as to whether a cloud computing arrangement (e.g., software as a service, platform as a service, infrastructure as a service, and other similar arrangements) includes a software license, and based on that determination, how to account for such arrangements.

We adopted this standard effective July 1, 2016 on a prospective basis. The adoption of this standard did not have a material impact on our financial statements.

In November 2015, the FASB issued an accounting standard update which requires that all deferred tax assets and liabilities, along with any related valuation allowance, be classified as noncurrent in the balance sheet. As a result, each separate tax jurisdiction will have one net tax position, either a noncurrent deferred tax asset or a noncurrent deferred tax liability. The standard is effective for us on July 1, 2017, with early adoption permitted. We elected to adopt this standard as of July 1, 2016 on a prospective basis. If we had adopted the standard retrospectively, the impact would have resulted in a \$6.2 million reduction to current deferred tax assets and noncurrent deferred tax liabilities in our June 30, 2016 balance sheet. The adoption of this standard did not have an impact on our statements of comprehensive loss or cash flows.

#### *Recent Accounting Pronouncements*

In May 2014, the FASB issued an accounting standard update which provides for new revenue recognition guidance, superseding nearly all existing revenue recognition guidance. The core principle of the new guidance is to recognize revenue when promised goods or services are transferred to customers, in an amount that reflects the consideration to which the vendor expects to receive for those goods or services. The new standard is expected to require more judgment and estimates within the revenue recognition process than required under existing US GAAP, including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to separate performance obligations. The new standard is also expected to significantly increase the financial statement disclosure related to revenue recognition. This standard is currently effective for us on July 1, 2018 (the first quarter of our fiscal year ending June 30, 2019 (fiscal

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year 2019)) using one of two methods of adoption: (i) retrospective to each prior reporting period presented, with the option to elect certain practical expedients as defined within the standard; or (ii) modified retrospective with the cumulative effect of initially applying the standard recognized at the date of initial application inclusive of certain additional disclosures.

We are continuing to evaluate the expected impact of this standard on our consolidated financial statements and we have not yet selected a method of adoption. While our assessment of the impact of this standard is not complete, we currently believe that the most significant impact will be in two specific areas:

Under the new standard, the absence of vendor specific objective evidence (VSOE) in certain software license arrangements will no longer result in strict revenue deferral, as instead fair value will be assigned to arrangement elements based on a fair value hierarchy no longer dependent on the presence of VSOE. Absent a change in how we license our products, we believe that this will result in greater up-front recognition of software revenue for certain of our license arrangements.

Under the new standard, certain expenses we incur will require deferral and recognition over the period in which revenue is recognized, subject to certain exceptions. We believe that this will result in the deferral of certain implementation and commission costs associated with our SaaS offerings which would then be recognized as expense over a multi-year period; such costs are expensed directly as incurred today.

However, we are unable to quantify the impact of these outcomes at this time, nor can we ensure that our continuing analysis and interpretation of the standard will result in this financial reporting outcome.

In January 2016, the FASB issued an accounting standard update which requires, among other things, that entities measure equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) at fair value, with changes in fair value recognized in earnings. Under the standard, entities will no longer be able to recognize unrealized holding gains and losses on equity securities classified today as available for sale as a component of other comprehensive income. For equity investments without readily determinable fair values, the cost method of accounting is also eliminated; however subject to certain exceptions, entities will be able to elect to record equity investments without readily determinable fair values at cost, less impairment and plus or minus adjustments for observable price changes, with all such changes recognized in earnings. This new standard does not change the guidance for classifying and measuring investments in debt securities and loans. The standard is effective for us on July 1, 2018 (the first quarter of fiscal year 2019) on a prospective basis. We are currently evaluating the anticipated impact of this standard on our financial statements.

In February 2016, the FASB issued an accounting standard update which requires balance sheet recognition of a lease liability and a corresponding right-of-use asset, with an optional policy election for short-term leases (i.e. leases with a term of 12 months or less that do not include options to purchase the underlying lease assets that the lessee is reasonably certain to exercise) under which a right-of-use asset and lease liability would not be recognized and short-term lease payments would be expensed on a straight line basis over the term of the lease. The amendments to this accounting standard also require new financial statement disclosures. This standard is effective for us on July 1, 2019 (the first quarter of the fiscal year ending June 30, 2020) with early adoption permitted; adoption is on a modified retrospective basis. We anticipate that upon adoption this standard will have a material impact to our consolidated balance sheet due to the recognition of right of use assets and lease liabilities; however we are still evaluating the anticipated impact of this standard on our financial statements.

In March 2016, the FASB issued an accounting standard update intended to simplify several areas of accounting for share-based compensation arrangements, including the income tax impact of excess tax benefits and tax deficiencies, accounting for forfeitures, statutory tax withholding requirements and the presentation of excess tax benefits in the statement of cash flows. This standard is effective for us on July 1, 2017 (the first quarter of the fiscal year ending June 30, 2018) with early adoption permitted. We are currently evaluating the anticipated impact of this standard on our financial statements.

In June 2016, the FASB issued an accounting standard update that introduces a new forward-looking approach, based on expected losses, to estimate credit losses on certain types of financial instruments including trade receivables. The estimate of expected credit losses will require entities to incorporate historical information, current information and reasonable and supportable forecasts. This standard also expands the disclosure requirements to enable users of financial statements to understand the entity's assumptions, models and methods for estimating expected credit losses. This standard is effective for us on July 1, 2020 (the first quarter of the fiscal year ending June 30, 2021) with early application permitted. We are currently evaluating the anticipated impact of this standard on our financial statements.

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In August 2016, the FASB issued an accounting standard update that provides guidance on how certain cash receipts and payments are presented and classified in the statement of cash flows. The standard is intended to reduce current diversity in practice. The standard is effective for us on July 1, 2018 and requires a retrospective approach. Early adoption is permitted, including adoption in an interim period. We are currently evaluating the anticipated impact of this standard on our financial statements.

**Note 3 Fair Value***Fair Values of Assets and Liabilities*

We measure fair value at the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the assumptions that market participants would use in pricing an asset or liability (the inputs) are based on a tiered fair value hierarchy consisting of three levels, as follows:

Level 1: Observable inputs such as quoted prices for identical assets or liabilities in active markets.

Level 2: Other inputs that are observable directly or indirectly, such as quoted prices for similar instruments in active markets or for similar markets that are not active.

Level 3: Unobservable inputs for which there is little or no market data and which require us to develop our own assumptions about how market participants would price the asset or liability.

Valuation techniques for assets and liabilities include methodologies such as the market approach, the income approach or the cost approach, and may use unobservable inputs such as projections, estimates and management's interpretation of current market data. These unobservable inputs are only utilized to the extent that observable inputs are not available or cost-effective to obtain.

At September 30, 2016 and June 30, 2016, our assets and liabilities measured at fair value on a recurring basis were as follows:

(in thousands)	September 30, 2016				June 30, 2016			
	Fair Value Measurements Using				Fair Value Measurements Using			
	Input Types				Input Types			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Money market funds (cash and cash equivalents)	\$ 235	\$	\$	\$ 235	\$ 117	\$	\$	\$ 117
Available for sale securities								
Debt								
US Corporate	\$ 10,888			\$ 10,888	\$ 9,580			\$ 9,580
Residential mortgage-backed	7,607			7,607	9,604			9,604
Government - US	10,621			10,621	15,962			15,962
Total available for sale securities	\$ 29,116	\$	\$	\$ 29,116	\$ 35,146	\$	\$	\$ 35,146

*Fair Value of Financial Instruments*

We have certain financial instruments which consist of cash and cash equivalents, marketable securities, accounts receivable, accounts payable and convertible senior notes (the Notes) more fully described in Note 10. Fair value information for each of these instruments is as follows:

Cash and cash equivalents, accounts receivable and accounts payable fair value approximates their carrying values, due to the short-term nature of these instruments.

Marketable securities classified as held to maturity are recorded at amortized cost, which at September 30, 2016 and June 30, 2016, approximated fair value.

Marketable securities classified as available for sale are recorded at fair value. Unrealized gains and losses are included as a component of other accumulated comprehensive loss in shareholders' equity, net of tax. We use the specific identification method to determine any realized gains or losses from the sale of our marketable securities classified as available for sale.

The carrying value of assets (\$1.5 million and \$1.4 million) related to deposits we have made to fund future requirements associated with Israeli severance arrangements approximated their fair value at September 30, 2016 and June 30, 2016, respectively.

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We have certain other investments accounted for at cost. The carrying value of these investments was \$7.7 million at both September 30, 2016 and June 30, 2016 and they are reported as a component of our other assets. These investments are recorded at cost less any write-downs for other-than-temporary impairment charges. To determine the fair value of these investments, we use all available financial information including information based on recent or pending third-party equity investments in these entities. In certain instances, a cost method investment's fair value may not be estimated if there are no identified events or changes in circumstances that would indicate a significant adverse effect on the fair value of the investment and to do so would be impractical.

The Notes were recorded at \$133.3 million upon issuance, which reflected their principal value less the fair value of the embedded conversion option (Conversion Feature). The carrying value (net of debt issuance costs) of the Notes, \$173.2 million at September 30, 2016, will be accreted over the remaining term to maturity to their principal value of \$189.8 million. The fair value of the Notes (inclusive of the Conversion Feature) was approximately \$194.0 million as of September 30, 2016. We estimated the fair value of the Notes by reference to quoted market prices; however the Notes have only a limited trading volume and as such this fair value estimate is not necessarily the value at which the Notes could be retired or transferred.

*Marketable Securities*

The table below presents information regarding our marketable securities by major security type as of September 30, 2016 and June 30, 2016.

	September 30, 2016			June 30, 2016		
	Held to Maturity	Available for Sale	Total	Held to Maturity	Available for Sale	Total
(in thousands)						
Marketable securities:						
Corporate and other debt securities	66	29,116	29,182	63	35,146	35,209
<b>Total marketable securities</b>	<b>\$ 66</b>	<b>\$ 29,116</b>	<b>\$ 29,182</b>	<b>\$ 63</b>	<b>\$ 35,146</b>	<b>\$ 35,209</b>

The following table summarizes the estimated fair value of our investments in available for sale marketable securities classified by the contractual maturity date of the securities:

	September 30, 2016
	(in thousands)
Due within 1 year	\$ 13,848
Due in 1 year through 5 years	\$ 15,268
<b>Total</b>	<b>\$ 29,116</b>

All of our available for sale marketable securities are included in current assets as we do not have the positive intent to hold these investments until maturity.



The following table presents the aggregate fair values and gross unrealized losses for those available for sale investments that were in an unrealized loss position as of September 30, 2016, aggregated by investment category and the length of time that individual securities have been in a continuous loss position:

	<b>At September 30, 2016</b>	
	<b>Less than 12 Months</b>	
	<b>Fair Value</b>	<b>Unrealized Loss</b>
	<b>(in thousands)</b>	
US Corporate	\$ 8,752	\$ 7
Residential mortgage-backed	\$ 3,458	\$ 5
Government US	\$ 498	\$
Total	\$ 12,708	\$ 12

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In December 2015, we made a \$3.5 million investment in preferred stock of a privately held, early-stage technology company. We have the ability to exercise significant influence over this company; however, we have no ability to exert control. Investments in common stock or in-substance common stock, through which an investor has the ability to exercise significant influence over the operating or financial policies of the investee, are accounted for under the equity method of accounting. In-substance common stock is an investment that has risk and reward characteristics that are substantially similar to an entity's common stock. The preferred stock underlying our investment is not in-substance common stock as its terms include a substantive liquidation preference not available to common stockholders. Accordingly, we accounted for our investment under the cost method of accounting, subject to periodic review for impairment. Impairment losses, to the extent occurring, would be recorded as an operating expense in the period incurred. Our maximum exposure, which is determined based on the cost of our investment, is \$3.5 million as of September 30, 2016. There were no indicators of impairment identified as of September 30, 2016.

We concluded that this company is a variable interest entity (VIE) as it lacks sufficient equity to finance its activities. However, we also concluded that we are not the primary beneficiary of the VIE as we do not have the power to exert control or direct the activities that most significantly impact the VIE's economic performance. As we have determined we are not the primary beneficiary, consolidation of the VIE is not required.

**Note 5 Net Loss Per Share**

The following table sets forth the computation of basic and diluted net loss per share:

	<b>Three Months Ended September 30, 2016                  2015 (in thousands except per share data)</b>	
<b>Numerator - basic and diluted:</b>		
Net loss	\$ (10,508)	\$ (4,253)
<b>Denominator:</b>		
Shares used in computing basic and diluted net loss per share attributable to common stockholders	37,940	38,004
<b>Basic and diluted net loss per share attributable to common stockholders</b>	<b>\$ (0.28)</b>	<b>\$ (0.11)</b>

For the three months ended September 30, 2016 and September 30, 2015, approximately 3.3 million and 3.1 million shares of unvested restricted stock and stock options, respectively, were excluded from the calculation of diluted earnings per share as their effect on the calculation would have been anti-dilutive.

As more fully discussed in Note 10, in December 2012 we issued the Notes maturing in December 2017. We intend, upon conversion or maturity of the Notes, to satisfy any conversion premium by issuing shares of our common stock.

We have also issued warrants for up to 6.3 million shares of our common stock at an exercise price of \$40.04 per share. For the quarter ended September 30, 2016, shares potentially issuable upon conversion or maturity of the Notes or upon exercise of the warrants were excluded from our earnings per share calculations as their effect would have been anti-dilutive.

## **Note 6 Operations by Segments and Geographic Areas**

### *Segment Information*

Operating segments are the components of our business for which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Our chief operating decision maker is our chief executive officer. Our operating segments are organized principally by the type of product or service offered and by geography.

During the fiscal year ended June 30, 2016 (fiscal year 2016), we re-examined the aggregation of our operating segments and reclassified our cyber fraud and risk management and healthcare operating segments from the Payments and Transactional Documents reportable segment into the new Other reportable segment. To ensure a consistent presentation of the measurement of segment revenues and profit or loss, these changes are reflected for all periods presented.

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Similar operating segments have been aggregated into four reportable segments as follows:

*Payments and Transactional Documents.* Our Payments and Transactional Documents segment is a supplier of software products that provide a range of financial business process management solutions including making and collecting payments, sending and receiving invoices, and generating and storing business documents. This segment also incorporates our payments automation software for direct debit and receivables management and provides a range of standard professional services and equipment and supplies that complement and enhance our core software products. Revenue associated with the aforementioned products and services is typically recorded upon delivery. This segment also incorporates certain other solutions that are licensed on a subscription basis, revenue for which is typically recorded on a subscription or transaction basis, or ratably over the expected life of the customer relationship.

*Hosted Solutions.* Our Hosted Solutions segment provides customers predominately with SaaS technology offerings that facilitate electronic payment, electronic invoicing, and spend management. Our legal spend management solutions, which enable customers to create more efficient processes for managing invoices generated by outside law firms while offering insight into important legal spend factors such as expense monitoring and outside counsel performance, are included within this segment. This segment incorporates our global financial messaging and Paymode-X solutions. Revenue within this segment is generally recognized on a subscription or transaction basis or ratably over the estimated life of the customer relationship.

*Digital Banking.* Our Digital Banking segment provides solutions that are specifically designed for banking and financial institution customers. Our Digital Banking products are now sold almost entirely on a subscription basis which has the effect of contributing to recurring subscription and transaction revenue and the revenue predictability of future periods, but which also delays revenue recognition over a longer period.

*Other.* Our Other segment consists of our healthcare and cyber fraud and risk management operating segments. Our cyber fraud and risk management solutions non-invasively monitor, replay and analyze user behavior to flag and even stop suspicious activity in real time. Our healthcare solutions for patient registration, electronic signature, mobile document and payments allow healthcare organizations to improve business efficiencies, reduce costs and improve care quality. When licensed on a perpetual license basis, revenue for our cyber fraud and risk management and healthcare products is typically recorded upon delivery, with the exception of software maintenance which is normally recorded ratably over a twelve month period. When products are licensed on a subscription basis, revenue is normally recorded ratably over the subscription period.

Periodically a sales person in one operating segment will sell products and services that are typically sold within a different operating segment. In such cases, the transaction is generally recorded by the operating segment to which the sales person is assigned. Accordingly, segment results can include the results of transactions that have been allocated to a specific segment based on the contributing sales resources, rather than the nature of the product or service. Conversely, a transaction can be recorded by the operating segment primarily responsible for delivery to the customer, even if the sales person is assigned to a different operating segment.

Our chief operating decision maker assesses segment performance based on a variety of factors that normally include segment revenue and a segment measure of profit or loss. Each segment's measure of profit or loss is on a pre-tax basis and excludes stock compensation expense, acquisition and integration related expenses (including acquisition related contingent consideration), amortization of acquired intangible assets, restructuring related charges, minimum pension liability adjustments, non-core charges related to our convertible notes, global enterprise resource planning (ERP) system implementation costs, charges related to reserves established or released against our deferred tax assets and other non-core or non-recurring gains and losses that arise from time to time. There are no inter-segment sales; accordingly, the measure of segment revenue and profit or loss reflects only revenues from external customers. The

costs of certain corporate level expenses, primarily general and administrative expenses, are allocated to our operating segments based on a percentage of the segment's revenues.

We do not track or assign our assets by operating segment.

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Segment information for the three months ended September 30, 2016 and 2015 according to the segment descriptions above, is as follows:

	<b>Three Months Ended September 30,</b>	
	<b>2016</b>	<b>2015</b>
	<b>(in thousands)</b>	
<b>Segment revenue:</b>		
Payments and Transactional Documents	\$ 24,846	\$ 27,416
Hosted Solutions	35,557	33,870
Digital Banking	18,186	17,331
Other	4,495	4,264
<b>Total segment revenue</b>	<b>\$ 83,084</b>	<b>\$ 82,881</b>
<b>Segment measure of profit (loss):</b>		
Payments and Transactional Documents	\$ 7,576	\$ 7,790
Hosted Solutions	5,453	6,574
Digital Banking	25	1,863
Other	(445)	(908)
<b>Total measure of segment profit</b>	<b>\$ 12,609</b>	<b>\$ 15,319</b>

A reconciliation of the measure of segment profit to GAAP loss before income taxes is as follows:

	<b>Three Months Ended September 30,</b>	
	<b>2016</b>	<b>2015</b>
	<b>(in thousands)</b>	
Total measure of segment profit	\$ 12,609	\$ 15,319
<b>Less:</b>		
Amortization of acquired intangible assets	(6,285)	(7,279)
Stock-based compensation expense	(8,199)	(7,588)
Acquisition and integration related expenses	(1,249)	(110)
Restructuring expenses		(20)
Minimum pension liability and related adjustments	(277)	(36)
Global ERP system implementation costs	(2,491)	(257)
Other expense, net	(3,935)	(3,671)
<b>Loss before income taxes</b>	<b>\$ (9,827)</b>	<b>\$ (3,642)</b>

The following depreciation expense amounts are included in the segment measure of profit:

**Three Months Ended September 30,**  
**2016**                      **2015**  
**(in thousands)**

Depreciation and other amortization expense:		
Payments and Transactional Documents	\$ 805	\$ 692
Hosted Solutions	1,840	1,424
Digital Banking	1,370	858
Other	72	103
 Total depreciation and other amortization expense	 \$ 4,087	 \$ 3,077

**Table of Contents***Geographic Information*

We have presented geographic information about our revenues below. This presentation allocates revenue based on the point of sale, not the location of the customer. Accordingly, we derive revenues from geographic locations based on the location of the customer that would vary from the geographic areas listed here; particularly in respect of financial institution customers located in Australia for which the point of sale was North America.

	<b>Three Months Ended September 30,</b>	
	<b>2016</b>	<b>2015</b>
	<b>(in thousands)</b>	
North America	\$ 50,522	\$ 48,596
United Kingdom	20,831	22,832
Continental Europe	9,352	9,452
Asia-Pacific and Middle East	2,379	2,001
<b>Total revenues from unaffiliated customers</b>	<b>\$ 83,084</b>	<b>\$ 82,881</b>

Long-lived assets, excluding deferred tax assets and intangible assets, which are based on geographical location, were as follows:

	<b>September 30,</b>	<b>June 30,</b>
	<b>2016</b>	<b>2016</b>
	<b>(in thousands)</b>	
Long-lived assets:		
North America	\$ 57,821	\$ 55,208
United Kingdom	8,346	8,499
Continental Europe	1,980	1,924
Asia-Pacific and Middle East	2,109	2,080
<b>Total long-lived assets</b>	<b>\$ 70,256</b>	<b>\$ 67,711</b>

**Note 7 Income Taxes**

The income tax expense we record in any interim period is based on our estimated effective tax rate for the fiscal year in those tax jurisdictions in which we can reliably estimate our effective tax rate. The calculation of our estimated effective tax rate requires an estimate of pre-tax income by tax jurisdiction, as well as total tax expense for the fiscal year. Accordingly, this tax rate is subject to adjustment if, in subsequent interim periods, there are changes to our initial estimates of total tax expense or pre-tax income, including income by jurisdiction. For those tax jurisdictions for which we are unable to reliably estimate an overall effective tax rate, we calculate income tax expense based upon the actual effective tax rate for the year-to-date period.

We recorded income tax expense of \$0.7 million and \$0.6 million for the three months ended September 30, 2016 and 2015, respectively. The income tax expense for the three months ended September 30, 2016 was principally due to tax



expense associated with our US and UK operations, offset in part by a tax benefit associated with our Swiss and Israeli operations. Our tax expense for the three months ended September 30, 2016 was offset in part by a discrete tax benefit of approximately \$0.1 million from the enactment of legislation that decreased UK income tax rates. The US income tax expense was principally due to an increase in deferred tax liabilities for goodwill that is deductible for tax purposes but not amortized for financial reporting purposes. The income tax expense for the three months ended September 30, 2015 was principally due to tax expense associated with our US and UK operations, offset in part by a tax benefit associated with our Swiss and Israeli operations.

We currently anticipate that our unrecognized tax benefits will decrease within the next twelve months by approximately \$0.3 million as a result of the expiration of certain statutes of limitations associated with intercompany transactions subject to tax in multiple jurisdictions.

We record a deferred tax asset if we believe that it is more likely than not that we will realize a future tax benefit. Ultimate realization of any deferred tax asset is dependent on our ability to generate sufficient future taxable income in the appropriate tax jurisdiction before the expiration of carryforward periods, if any. Our assessment of deferred tax asset recoverability considers many different factors including historical and projected operating results, the reversal of existing deferred tax liabilities that provide a source of future taxable income, the impact of current tax planning strategies and the availability of future tax planning strategies. We establish a valuation allowance against any deferred tax asset for which we are unable to conclude that recoverability is more likely than not. This is inherently judgmental, since we are required to assess many different factors and evaluate as much objective evidence as we can in reaching an overall conclusion. The particularly sensitive component of our evaluation is our projection of future operating results since this relies heavily on our estimates of future revenue and expense levels by tax jurisdiction.

At September 30, 2016 we have recorded a \$29.5 million valuation allowance against certain deferred tax assets given the uncertainty of recoverability of these amounts.

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The following tables set forth the information for intangible assets subject to amortization and for intangible assets not subject to amortization.

	<b>As of September 30, 2016</b>			<b>Weighted Average</b>
	<b>Gross Carrying</b>	<b>Accumulated</b>	<b>Net Carrying</b>	<b>Remaining</b>
	<b>Amount</b>	<b>Amortization</b>	<b>Value</b>	<b>Life</b>
		<b>(in thousands)</b>		<b>(in years)</b>
<b>Amortized intangible assets:</b>				
Customer related	\$ 190,220	\$ (113,157)	\$ 77,063	9.4
Core technology	130,347	(67,003)	63,344	9.3
Other intangible assets	20,521	(13,928)	6,593	6.1
Capitalized software development costs	13,716	(1,735)	11,981	5.8
<b>Total</b>	<b>\$ 354,804</b>	<b>\$ (195,823)</b>	<b>\$ 158,981</b>	
<b>Unamortized intangible assets:</b>				
Goodwill			201,489	
<b>Total intangible assets</b>			<b>\$ 360,470</b>	

	<b>As of June 30, 2016</b>			<b>Weighted Average</b>
	<b>Gross Carrying</b>	<b>Accumulated</b>	<b>Net Carrying</b>	<b>Remaining</b>
	<b>Amount</b>	<b>Amortization</b>	<b>Value</b>	<b>Life</b>
		<b>(in thousands)</b>		<b>(in years)</b>
<b>Amortized intangible assets:</b>				
Customer related	\$ 190,549	\$ (110,356)	\$ 80,193	9.6
Core technology	130,434	(64,591)	65,843	9.5
Other intangible assets	20,469	(13,320)	7,149	6.1
Capitalized software development costs	12,993	(1,248)	11,745	6.0
<b>Total</b>	<b>\$ 354,445</b>	<b>\$ (189,515)</b>	<b>\$ 164,930</b>	
<b>Unamortized intangible assets:</b>				
Goodwill			202,028	
<b>Total intangible assets</b>			<b>\$ 366,958</b>	

Estimated amortization expense for fiscal year 2017 and subsequent fiscal years for acquired intangible assets is as follows:

	<b>(in thousands)</b>
2017	\$ 24,452
2018	20,550
2019	18,607
2020	16,523
2021	14,964
2022 and thereafter	58,189

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Estimated amortization expense for fiscal year 2017 and subsequent fiscal years for capitalized software development costs using a straight-line methodology is stated below. Each period we evaluate whether amortization expense using a ratio of revenue in the period to total expected revenue over the product's expected useful life would result in greater amortization than as calculated under a straight-line methodology and, if that were to occur, amortization in that period would be accelerated accordingly.

	<b>(in thousands)</b>
2017	\$ 2,035
2018	2,087
2019	2,087
2020	2,087
2021	2,086
2022 and thereafter	2,086

The following table represents a rollforward of our goodwill balances, by reportable segment, as follows:

	<b>Payments and Transactional Documents</b>	<b>Hosted Solutions</b>	<b>Digital Banking</b>	<b>Other</b>	<b>Total</b>
	<b>(in thousands)</b>				
Balance at June 30, 2016	\$ 60,852	\$ 89,573	\$ 35,880	\$ 15,723	\$ 202,028
Impact of foreign currency translation	(387)	(152)			(539)
Balance at September 30, 2016	\$ 60,465	\$ 89,421	\$ 35,880	\$ 15,723	\$ 201,489

We perform an impairment test for goodwill during the fourth quarter each fiscal year. Based on our most recent impairment testing, during the fourth quarter of the year ended June 30, 2016, the excess of fair value over the carrying value of our Intellinx reporting unit was 14%. Given the relatively narrow excess of fair value over carrying value, we believe that this reporting unit remains at a heightened risk of impairment. The carrying value of goodwill in the Intellinx reporting unit was \$12.0 million at September 30, 2016.

There can be no assurance that there will not be impairment charges in future periods as a result of future impairment reviews. To the extent that future impairment charges occur it would have a material impact on our financial results. At September 30, 2016, the carrying value of goodwill for all of our reporting units was \$201.5 million.

**Note 9 Contingencies**

During fiscal year 2016, we agreed to indemnify a customer against costs it may incur as a result of a lawsuit filed against them for alleged patent infringement related to certain technology licensed from us, which we license and resell from an outside supplier. We in turn received indemnification from the outside supplier. Bottomline was not named as a party to this lawsuit. In September 2016, we were notified by the supplier that the litigation had been resolved. We were not a party to the settlement, and neither we nor our customer incurred any monetary or other damages in connection therewith.

We are, from time to time, a party to legal proceedings and claims that arise out of the ordinary course of our business. We are not currently a party to any material legal proceedings.

#### **Note 10 - Convertible Senior Notes**

On December 12, 2012, we issued \$189.8 million aggregate principal amount of our 1.50% Convertible Senior Notes maturing on December 1, 2017 (the Notes), inclusive of the underwriters' exercise in full of their over-allotment option of \$24.8 million. Cash interest at a rate of 1.50% per year began to accrue on December 12, 2012 and is payable semi-annually on June 1 and December 1 of each year beginning on June 1, 2013. We received net proceeds from the offering of approximately \$167.3 million after adjusting for debt issue costs, including the underwriting discount, and the net cash used to purchase the Note Hedges and sell the Warrants which are discussed below.

The Notes were issued under an indenture dated December 12, 2012 (the Base Indenture) by and between us and The Bank of New York Mellon Trust Company, N.A., as Trustee and a First Supplemental Indenture dated December 12, 2012 (the First Supplemental Indenture) by and between us and the Trustee (the Base Indenture and the First Supplemental Indenture are collectively referred to as the Indenture). There are no financial or operating covenants relating to the Notes.

The Notes are senior unsecured obligations of ours and rank senior in right of payment to any future unsecured indebtedness that is expressly subordinated in right of payment to the Notes, and equal in right of payment to any of our existing and future unsecured indebtedness that is not subordinated. The Notes are effectively junior in right of payment to any of our secured indebtedness (to the extent of the value of assets securing such indebtedness) and structurally junior to all existing and future indebtedness and other liabilities, including trade payables, of our subsidiaries. Prior to this offering, neither we nor our subsidiaries had any outstanding indebtedness for borrowed money. The Indenture does not limit the amount of debt that we or our subsidiaries may incur. The Notes are not guaranteed by us or any of our subsidiaries.

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Holders may convert their Notes at their option, prior to the close of business on the business day immediately preceding June 1, 2017, in multiples of \$1,000 principal amount, only under the following circumstances:

during any calendar quarter commencing after the calendar quarter ending on March 31, 2013 (and only during such calendar quarter), if the last reported sale price of our common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter is greater than or equal to 130% of the conversion price on each applicable trading day;

during the five business day period after any five consecutive trading day period (the measurement period) in which the trading price per \$1,000 principal amount of the convertible notes for each trading day of the measurement period was less than 98% of the product of the last reported sales price of our common stock and the conversion rate on each trading day; or

upon the occurrence of specified corporate events, including a merger or a sale of all or substantially all of our assets.

On or after June 1, 2017 and until the close of business on the second scheduled trading day immediately preceding the maturity date of December 1, 2017, holders may convert their Notes, in multiples of \$1,000 principal amount, at the option of the holder regardless of the foregoing circumstances.

The conversion rate for the Notes is initially 33.3042 shares per \$1,000 principal amount of Notes (equivalent to an initial conversion price of approximately \$30.03 per share of our common stock). The conversion rate is subject to customary adjustment for certain events as described in the Indenture.

The principal balance of the Notes is always required to be settled in cash. However, we are permitted at our election to settle any conversion obligation in excess of the principal portion in cash, shares of our common stock, or a combination of cash and shares of our common stock.

We may not redeem the Notes prior to their maturity date. If we undergo a fundamental change (as described in the Indenture), subject to certain conditions, holders may require us to repurchase for cash all or part of their Notes in principal amounts of \$1,000 or an integral multiple thereof. The fundamental change repurchase price will be equal to 100% of the principal amount of the Notes to be repurchased, plus accrued and unpaid interest to, but excluding, the fundamental change repurchase date.

The Indenture contains customary events of default with respect to the Notes and provides that upon certain events of default occurring and continuing, the Trustee may, and the Trustee at the request of such holders of at least 25% in principal amount of the convertible notes shall, declare 100% of the principal of and accrued and unpaid interest, if any, on the Notes to be due and payable. In case of certain events of bankruptcy, insolvency or reorganization, involving us or a significant subsidiary, 100% of the principal of and accrued and unpaid interest on the Notes will automatically become due and payable. Upon such a declaration of acceleration, such principal and accrued and unpaid interest, if any, will be due and payable immediately.

Under limited circumstances, we may be required to pay contingent interest on the Notes as a result of failure to comply with the reporting obligations in the Indenture or failure to file required Securities and Exchange Commission

documents and reports. When applicable, the contingent interest payable per \$1,000 principal amount is 0.25% per annum over the applicable term as provided under the Indenture. The contingent interest features of the Notes are embedded derivative instruments. The estimated fair value of the contingent interest features of the Notes was zero at issuance and at September 30, 2016, as the likelihood of any liability being incurred under these provisions was deemed remote and, to the extent occurring, the time period during which a contingent interest charge would apply is projected to be short.

The Notes were recorded upon issuance using a residual method of valuation, meaning since the Conversion Feature was initially a derivative instrument recorded at fair value, we allocated debt proceeds to the Conversion Feature based on the fair value of that instrument and the residual proceeds were allocated to the Notes. The carrying amount of the Notes will be accreted to the principal amount over the remaining term to maturity and we will record a corresponding charge to interest expense.

The net carrying amount of the Notes at September 30, 2016 was as follows:

	<b>(in thousands)</b>
Principal amount	\$ 189,750
Unamortized debt issuance costs	(1,381)
Unamortized discount	(15,140)
Net carrying value	\$ 173,229

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We incurred certain third party costs in connection with our issuance of the Notes, principally related to underwriting and legal fees, which are being amortized to interest expense ratably over the five-year term of the Notes.

The following table sets forth total interest expense related to the Notes:

	<b>Three Months Ended September 30,</b>	
	<b>2016</b>	<b>2015</b>
	<b>(in thousands)</b>	
Contractual interest expense (cash)	\$ 712	\$ 712
Amortization of debt discount (non-cash)	3,076	2,865
Amortization of debt issue costs (non-cash)	296	296
	\$ 4,084	\$ 3,873
Effective interest rate of the liability component	7.99%	7.54%

*Note Hedges*

In December 2012, we entered into privately negotiated transactions to purchase hedge instruments (the Note Hedges), covering approximately 6.3 million shares of our common stock. The Note Hedges are subject to anti-dilution provisions substantially similar to those of the Notes, have a strike price that corresponds to the conversion price of the Notes, are exercisable by us upon any conversion under the Notes and expire on December 1, 2017.

The Note Hedges are generally expected to reduce the potential dilution to our common stock (or, in the event the Conversion Feature is settled in cash, to reduce our cash payment obligation) in the event that at the time of conversion our stock price exceeds the conversion price under the Notes. The cost of the Note Hedges, \$42.3 million, is expected to be tax deductible as an original issue discount over the life of the Notes, as the Notes and the Note Hedges represent an integrated debt instrument for tax purposes.

The Note Hedges are transactions that are separate from the terms of the Notes and the Warrants (discussed below), and holders of the Notes and the Warrants have no rights with respect to the Note Hedges.

*Warrants*

In December 2012, we received aggregate proceeds of \$25.8 million, net of issue costs, from the sale of warrants (the Warrants), for the purchase of up to 6.3 million shares of our common stock, subject to antidilution adjustments, at a strike price of \$40.04 per share. The Warrants are exercisable in equal tranches over a period of 150 days beginning on March 1, 2018, and ending on October 18, 2018.

The Warrants are transactions that are separate from the terms of the Notes and the Note Hedges, and holders of the Notes and Note Hedges have no rights with respect to the Warrants.

**Note 11 Derivative Instruments**



Our derivative instruments for the quarter ended September 30, 2016 consisted of the Note Hedges, Conversion Feature and Warrants as discussed in Note 10. As of September 30, 2016, each of these instruments continued to meet the classification requirements for inclusion within stockholders' equity and as such they were not subject to fair value re-measurement. We are required, for the remaining term of the Notes, to assess whether we continue to meet the stockholders' equity classification requirements. If in any future period we failed to satisfy those requirements, we would be required to reclassify the derivative instruments out of stockholders' equity, to either assets or liabilities depending on their nature, and record those instruments at fair value with changes in fair value reflected in earnings.

## **Note 12 Postretirement and Other Employee Benefits**

### *Defined Benefit Pension Plan*

We sponsor a retirement plan for our Swiss-based employees that is governed by local regulatory requirements. This plan includes certain minimum benefit guarantees that, under US GAAP, require defined benefit plan accounting.

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Net periodic pension costs for the Swiss pension plan include the following components:

	<b>Three Months Ended September 30,</b>	
	<b>2016</b>	<b>2015</b>
	<b>(in thousands)</b>	
<b>Components of net periodic cost</b>		
Service cost	\$ 750	\$ 578
Interest cost	32	123
Prior service credit	(23)	(23)
Net actuarial loss	165	18
Expected return on plan assets	(224)	(204)
<b>Net periodic cost</b>	<b>\$ 700</b>	<b>\$ 492</b>

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

This Quarterly Report on Form 10-Q contains forward-looking statements that involve risks and uncertainties. The statements contained in this report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). Without limiting the foregoing, the words may, will, should, could, expects, plans, intends, anticipates, believes, estimates, predicts, potential and similar expressions are intended to identify forward-looking statements. All forward-looking statements included in this Quarterly Report on Form 10-Q are based on information available to us up to and including the date of this report, and we assume no obligation to update any such forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth below under Management's Discussion and Analysis of Financial Condition and Results of Operations and Item 1A. Risk Factors and elsewhere in this Form 10-Q. You should carefully review those factors and also carefully review the risks outlined in other documents that we file from time to time with the Securities and Exchange Commission.

In the management discussion that follows, we have highlighted those changes and operating factors that were the primary factors affecting period to period fluctuations. The remainder of the change in period to period fluctuations from that which is specifically disclosed arises from various individually insignificant items.

#### **Overview**

We help businesses pay and get paid. We make complex business payments simple, secure and seamless by providing a trusted and easy-to-use set of cloud-based business payment, digital banking, fraud prevention, payment and financial document solutions. We offer hosted or Software as a Service (SaaS) solutions, as well as software designed to run on-site at the customer's location. The majority of our revenues are derived from offerings sold as SaaS-based solutions and paid for on a subscription and transaction basis.

We operate a cloud-based network that facilitates the exchange of electronic payments between businesses and their vendors. We offer hosted and on-premise solutions that banks use to provide payment, cash management and treasury capabilities to their business customers, as well as solutions that banks and credit unions use to facilitate customer acquisition and growth. We offer financial messaging solutions for banks and corporations around the world, via solutions that leverage the SWIFT global messaging network. We also offer legal spend management solutions that help manage and determine the right amount to pay for legal services and claims vendor expenditures for insurance companies and other large corporate consumers of outside legal services. Our corporate customers rely on our solutions to automate their payment and accounts payable processes and to streamline and manage the production and retention of electronic documents. Our healthcare customers use our solutions to streamline financial processes, particularly the patient enrollment process. Our document automation solutions are used by organizations to automate paper-intensive processes for the generation of transactional and supply chain documents. We also offer comprehensive cyber fraud and risk management solutions that are designed to non-invasively monitor and analyze user behavior to flag behavioral and data anomalies and other suspicious activity.

Our solutions are designed to complement, leverage and extend our customers' existing information systems, accounting applications and banking relationships so that they can be deployed quickly and efficiently. To help our customers realize the maximum value from our products and meet their specific business requirements, we also provide professional services for installation, training, consulting and product enhancement.

#### *Financial Highlights*

For the three months ended September 30, 2016, our revenue increased to \$83.1 million from \$82.9 million in the same period of the prior year. This revenue increase was attributable to revenue increases in our Hosted Solutions segment (\$1.7 million), Digital Banking segment (\$0.9 million) and Other segment (\$0.2 million), partially offset by decreased revenue in our Payments and Transactional Documents segment (\$2.6 million). Increased revenue from our legal spend management and Paymode-X solutions accounted for the revenue increase in our Hosted Solutions segment. The Digital Banking segment's revenue increase was primarily due to increased subscription and transaction revenue from our cloud based solutions. The revenue decrease in our Payments and Transactional Documents segment was related to lower European and North American software license revenue and service and maintenance revenue in our payment and document automation products. Our revenue for the three months ended September 30, 2016 was unfavorably impacted by \$3.7 million due to the impact of foreign currency exchange rates primarily related to the British Pound Sterling which depreciated against the US Dollar as compared to the prior year.

We incurred a net loss of \$10.5 million in the three months ended September 30, 2016 compared to a net loss of \$4.3 million in the same period of the prior year. Our net loss for the three months ended September 30, 2016 was affected by the impact of decreased gross margins of \$2.6 million and increased operating expenses of \$3.3 million. The decrease in gross margins was primarily driven

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by decreases in our Payments and Transactional Documents and Digital Banking segments. The increase in our operating expenses was due primarily to increased employee related costs as we continued to grow our business, global enterprise resource planning (ERP) implementation costs of \$2.5 million and increased acquisition related costs of \$1.1 million.

In the three months ended September 30, 2016, we derived approximately 40% of our revenue from customers located outside of North America, principally in the United Kingdom, continental Europe and the Asia-Pacific region.

We expect future revenue growth to be driven by our digital banking, legal spend management, financial messaging and Paymode-X solutions.

Over the past several years we have made strategic investments in innovative new technology offerings that we believe will enhance our competitive position, help us win new business, drive subscription revenue growth and expand our operating margins. We believe that these initiatives have positioned us effectively for revenue growth in future years.

## **Critical Accounting Policies and Significant Judgments and Estimates**

We believe that several accounting policies are important to understanding our historical and future performance. We refer to these policies as critical because these specific areas generally require us to make judgments and estimates about matters that are uncertain at the time we make the estimate, and different estimates which also would have been reasonable could have been used.

The critical accounting policies we identified in our most recent Annual Report on Form 10-K for the fiscal year ended June 30, 2016 related to revenue recognition, the valuation of goodwill and intangible assets, the valuation of acquired deferred revenue and income taxes. There have been no material changes to the critical accounting policies disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2016. It is important that the discussion of our operating results that follows be read in conjunction with the critical accounting policies disclosed in our Annual Report on Form 10-K, as filed with the SEC on August 29, 2016.

## **Recent Accounting Pronouncements**

For information with respect to recent accounting pronouncements and the impact of these pronouncements on our consolidated financial statements, see Note 2, Recent Accounting Pronouncements, of the Notes to the Unaudited Condensed Consolidated Financial Statements.

## **Results of Operations**

### **Three Months Ended September 30, 2016 Compared to the Three Months Ended September 30, 2015**

#### ***Segment Information***

Operating segments are components of an enterprise for which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Our chief operating decision maker is our chief executive officer.

Our operating segments are organized principally by the type of product or service offered and by geography. Similar operating segments have been aggregated into four reportable segments: Payments and Transactional Documents,

Hosted Solutions, Digital Banking and Other.

During the fiscal year ended June 30, 2016, we re-examined the aggregation of our operating segments and reclassified our cyber fraud and risk management and healthcare operating segments from the Payments and Transactional Documents reportable segment into the new Other reportable segment. To ensure a consistent presentation of the measurement of segment revenues and profit or loss, these changes are reflected for all periods presented.

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The following tables represent our segment revenues and our segment measure of profit:

	Three Months Ended September 30,		Increase (Decrease) Between Periods	
	2016	2015	2016 compared to 2015	%
	(in thousands)			
<b>Segment revenue:</b>				
Payments and Transactional Documents	\$ 24,846	\$ 27,416	\$ (2,570)	(9.4)
Hosted Solutions	35,557	33,870	1,687	5.0
Digital Banking	18,186	17,331	855	4.9
Other	4,495	4,264	231	5.4
	\$ 83,084	\$ 82,881	\$ 203	0.2
<b>Segment measure of profit:</b>				
Payments and Transactional Documents	\$ 7,576	\$ 7,790	(214)	(2.7)
Hosted Solutions	5,453	6,574	(1,121)	(17.1)
Digital Banking	25	1,863	(1,838)	(98.7)
Other	(445)	(908)	463	51.0
Total measure of segment profit	\$ 12,609	\$ 15,319	\$ (2,710)	(17.7)

A reconciliation of the measure of segment profit to our GAAP loss for the three months ended September 30, 2016 and September 30, 2015, before the provision for income taxes, is as follows:

	Three Months Ended September 30,	
	2016	2015
	(in thousands)	
Total measure of segment profit	\$ 12,609	\$ 15,319
Less:		
Amortization of acquired intangible assets	(6,285)	(7,279)
Stock-based compensation expense	(8,199)	(7,588)
Acquisition and integration related expenses	(1,249)	(110)
Restructuring expenses		(20)
Minimum pension liability and related adjustments	(277)	(36)
Global ERP system implementation costs	(2,491)	(257)
Other expense, net	(3,935)	(3,671)
Loss before income taxes	\$ (9,827)	\$ (3,642)

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*Payments and Transactional Documents.* Revenues for the three months ended September 30, 2016, as compared to the same period in the prior fiscal year, were unfavorably impacted by \$2.4 million due to the impact of foreign currency exchange rates. The overall revenue decrease of \$2.6 million, inclusive of the impact of unfavorable foreign currency exchange rates, was primarily attributable to revenue decreases of \$2.6 million in service and maintenance revenue, \$1.0 million in software license revenue and \$0.4 million in other revenue, partially offset by increases of \$1.4 million in subscriptions and transactions revenue. The segment profit decrease of \$0.2 million for the three months ended September 30, 2016, as compared to the same period in the prior fiscal year, including an unfavorable impact of foreign currency exchange rates of \$0.6 million, was primarily attributable to the revenue decrease described above, partially offset by decreased cost of sales of \$0.9 million and decreased operating expenses of \$1.4 million. We expect revenue and profit for the Payments and Transactional Documents segment to remain consistent during the remainder of fiscal year 2017.

*Hosted Solutions.* Revenues from our Hosted Solutions segment increased \$1.7 million for the three months ended September 30, 2016 as compared to the same period in the prior fiscal year, inclusive of an unfavorable impact of foreign currency exchange rates of \$1.2 million, due primarily to increased revenue from our legal spend management and Paymode-X solutions, partially offset by revenue decreases from our financial messaging solutions. Segment profit decreased \$1.1 million as compared to the same period in the prior fiscal year, inclusive of an unfavorable impact of foreign currency exchange rates of \$0.4 million, due primarily to decreased gross margins from our financial messaging solutions and increased operating expenses of \$1.0 million primarily related to increased product development costs. We expect revenue and profit for the Hosted Solutions segment to increase during the remainder of the fiscal year as a result of the continued revenue contribution from our legal spend management, financial messaging and Paymode-X solutions.

*Digital Banking.* Revenues from our Digital Banking segment increased \$0.9 million for the three months ended September 30, 2016 as compared to the same period in the prior fiscal year due to increases of \$2.1 million in subscription and transaction revenue, partially offset by decreased software license revenue of \$1.1 million. Segment profit decreased \$1.8 million for the three months ended September 30, 2016 as compared to the same period in the prior fiscal year, due primarily to decreased gross margins and increased product development costs of \$0.9 million. We expect revenue and profit for the Digital Banking segment to increase slightly for the remainder of the fiscal year as the Digital Banking segment continues to transition customers to hosted offerings and as more customers go live with the hosted offerings.

*Other.* Revenues from our Other segment increased \$0.2 million for the three months ended September 30, 2016 compared to the same period in the prior fiscal year. We expect Other revenue to decrease slightly during the remainder of the fiscal year.

**Revenues by category**

	Three Months Ended September 30,				Increase (Decrease) Between Periods	
	2016		2015		2016 Compared to 2015	
	(in thousands)	As % of total Revenues	(in thousands)	As % of total Revenues	(in thousands)	%
Revenues:						
Subscriptions and transactions	\$ 52,132	62.7	\$ 46,197	55.7	\$ 5,935	12.8



Software licenses	2,121	2.6	4,115	5.0	(1,994)	(48.5)
Service and maintenance	27,673	33.3	30,784	37.1	(3,111)	(10.1)
Other	1,158	1.4	1,785	2.2	(627)	(35.1)
Total revenues	\$ 83,084	100.0	\$ 82,881	100.0	\$ 203	0.2

*Subscriptions and Transactions.* Revenues for the three months ended September 30, 2016 were unfavorably impacted by \$1.5 million due to the impact of foreign currency exchange rates. The overall revenue increase of \$5.9 million, inclusive of the impact of unfavorable foreign currency exchange rates for the three months ended September 30, 2016, as compared to the same period in the prior fiscal year, was due principally to increases in revenue contribution from our Digital Banking segment of \$2.1 million and increases in revenue from our legal spend management and Paymode-X solutions. We expect subscriptions and transactions revenues to increase during the remainder of the fiscal year, primarily as a result of increased revenue from our legal spend management, financial messaging, digital banking and Paymode-X solutions.

*Software Licenses.* Revenue from software licenses decreased in the three months ended September 30, 2016 as compared to the same period in the prior fiscal year, primarily as a result decreases in revenue from our Digital Banking segment of \$1.1 million and decreases in North American payments and transactional documents revenue of \$0.6 million and European payments and transactional documents revenue of \$0.3 million. We expect software license revenues to increase during the remainder of fiscal year 2017, principally as a result of increased software license revenue from our Payments and Transactional Documents segment.

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*Service and Maintenance.* Service and maintenance revenues for the three months ended September 30, 2016 were unfavorably impacted by \$1.7 million due to the impact of foreign exchange rates. The overall decrease in service and maintenance revenues, inclusive of the impact of foreign currency exchange rates, for the three months ended September 30, 2016 as compared to the same period in the prior fiscal year was primarily the result of decreases in revenue from our European payments and transactional documents solutions of \$1.8 million, our North American payments and transactional documents solutions of \$0.8 million and collectively from our financial messaging solutions of \$0.6 million. We expect that service and maintenance revenues will decrease during the remainder of the fiscal year primarily as a result of our continued de-emphasis of customized digital banking projects.

*Other.* Our other revenues consist principally of equipment and supplies sales which remained minor components of our overall revenue. We expect that other revenues will remain relatively consistent during the remainder of the fiscal year.

**Cost of revenues by category**

	Three Months Ended September 30, 2016		2015		Increase (Decrease) Between Periods 2016 Compared to 2015	
	(in thousands)	As % of total Revenues	(in thousands)	As % of total Revenues	(in thousands)	%
Cost of revenues:						
Subscriptions and transactions	\$ 23,886	28.7	\$ 20,734	25.0	\$ 3,152	15.2
Software licenses	128	0.1	288	0.3	(160)	(55.6)
Service and maintenance	13,285	16.0	12,978	15.7	307	2.4
Other	878	1.1	1,335	1.6	(457)	(34.2)
Total cost of revenues	\$ 38,177	45.9	\$ 35,335	42.6	\$ 2,842	8.0

Gross profit	\$ 44,907	54.1	\$ 47,546	57.4	\$ (2,639)	(5.6)
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*Subscriptions and Transactions.* Subscriptions and transactions costs include salaries and other related costs for our professional services teams as well as costs related to our hosting infrastructure such as depreciation and facilities related expenses. Subscriptions and transactions costs increased slightly to 46% of subscription and transactions revenues in the three months ended September 30, 2016 compared to 45% of subscriptions and transactions revenues in the three months ended September 30, 2015, primarily due to decreased subscriptions and transactions gross margins in our financial messaging solutions, offset in part by increased gross margins in our legal spend management, Paymode-X and digital banking solutions. We expect that subscriptions and transactions costs will decrease slightly as a percentage of subscriptions and transactions revenue during the remainder of the fiscal year.

*Software Licenses.* Software license costs consist of expenses incurred by us to manufacture, package and distribute our software products and related documentation and costs of licensing third party software that is incorporated into or sold with certain of our products. Software license costs decreased slightly to 6% of software license revenues in the three months ended September 30, 2016 as compared to 7% of software license revenue in the three months ended September 30, 2015. We expect that software license costs will remain consistent, as a percentage of software license

revenues, during the remainder of the fiscal year.

*Service and Maintenance.* Service and maintenance costs include salaries and other related costs for our customer service, maintenance and help desk support staffs, as well as third party contractor expenses used to complement our professional services team. Service and maintenance costs increased to 48% of service and maintenance revenues in the three months ended September 30, 2016 as compared to 42% of service and maintenance revenues in the three months ended September 30, 2015. The increase in costs as a percent of service and maintenance revenues was driven principally by the decrease in service and maintenance revenue in our European and North American payments and transactional documents solutions. We expect that service and maintenance costs will increase slightly as a percentage of service and maintenance revenues, during the remainder of the fiscal year.

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*Other.* Other costs include the costs associated with equipment and supplies that we resell, as well as freight, shipping and postage costs associated with the delivery of our products and remain minor components of our business. We expect that other costs will remain relatively consistent as a percentage of other revenues for the remainder of the fiscal year.

**Operating Expenses**

	Three Months Ended September 30, 2016		2015		Increase (Decrease) Between Periods 2016 Compared to 2015	
	(in thousands)	As % of total Revenues	(in thousands)	As % of total Revenues	(in thousands)	%
Operating expenses:						
Sales and marketing	\$ 18,875	22.7	\$ 20,155	24.3	\$ (1,280)	(6.4)
Product development and engineering	12,935	15.6	11,260	13.6	1,675	14.9
General and administrative	12,704	15.3	8,823	10.6	3,881	44.0
Amortization of intangible assets	6,285	7.5	7,279	8.8	(994)	(13.7)
Total operating expenses	\$ 50,799	61.1	\$ 47,517	57.3	\$ 3,282	6.9

*Sales and Marketing.* Sales and marketing expenses consist primarily of salaries and other related costs for sales and marketing personnel, sales commissions, travel, public relations and marketing materials and trade show participation. Sales and marketing expenses decreased in the three months ended September 30, 2016 as compared to the three months ended September 30, 2015 primarily as a result of a decrease in employee related costs of \$0.7 million and decreases in advertising expenses of \$0.3 million and travel related expenses of \$0.2 million. We expect that sales and marketing expenses will remain relatively consistent over the remainder of the fiscal year.

*Product Development and Engineering.* Product development and engineering expenses consist primarily of personnel costs to support product development which consists of enhancements and revisions to our products based on customer feedback and general marketplace demands. Product development and engineering expenses in the three months ended September 30, 2016 as compared to the three months ended September 30, 2015 increased principally as a result of an increase in headcount related costs. We expect that product development and engineering expenses will remain relatively consistent during the remainder of the fiscal year as we continue to invest in our SaaS-based solutions that we believe will drive future revenue growth, such as our digital banking and legal spend management solutions as well as our European product offerings.

*General and Administrative.* General and administrative expenses consist primarily of salaries and other related costs for operations and finance employees and legal and accounting services. General and administrative expenses increased in the three months ended September 30, 2016 as compared to the three months ended September 30, 2015 primarily due to an increase in costs associated with global internal system implementations of \$2.2 million, increased acquisition related costs of \$1.0 million and increased employee related costs of \$0.7 million. We expect general and administrative expenses will increase during the remainder of the fiscal year, principally as a result of our on-going internal system initiatives.

*Amortization of Intangible Assets.* We amortize our acquired intangible assets in proportion to the estimated rate at which the asset provides economic benefit to us. Accordingly, amortization expense rates are often higher in the earlier periods of an asset's estimated life. The decrease in amortization expense in the three months ended September 30, 2016 as compared to the three months ended September 30, 2015 occurred as a result of amortization rates decreasing over the underlying asset lives. We expect that total amortization expense for acquired intangible assets for fiscal year 2017 will be approximately \$24.5 million.

### Other Expense, Net

	Three Months Ended September 30,		Increase (Decrease) Between	
	2016	2015	Periods	
	(in		2016 Compared to 2015	
	thousands)			%
Interest income	\$ 154	\$ 124	\$ 30	24.2
Interest expense	(4,040)	(3,835)	(205)	(5.3)
Other expense, net	(49)	40	(89)	(222.5)
Other expense, net	\$ (3,935)	\$ (3,671)	\$ (264)	(7.2)

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*Other Expense, Net.* For the three months ended September 30, 2016 as compared to the three months ended September 30, 2015, interest income increased slightly. The increase in interest expense is due to increased amortization of our debt discount. The decrease in other expense is due to an increase in foreign exchange rate losses incurred in the three months ended September 30, 2016 compared with the three months ended September 30, 2015.

**Provision for Income Taxes**

We recorded income tax expense of \$0.7 million and \$0.6 million for the three months ended September 30, 2016 and 2015, respectively. The income tax expense for the three months ended September 30, 2016 was principally due to tax expense associated with our US and UK operations, offset in part by a tax benefit associated with our Swiss and Israeli operations. Our tax expense for the three months ended September 30, 2016 was offset in part by a discrete tax benefit of approximately \$0.1 million from the enactment of legislation that decreased UK income tax rates. The US income tax expense was principally due to an increase in deferred tax liabilities for goodwill that is deductible for tax purposes but not amortized for financial reporting purposes. The income tax expense for the three months ended September 30, 2015 was principally due to tax expense associated with our US and UK operations, offset in part by a tax benefit associated with our Swiss and Israeli operations.

**Liquidity and Capital Resources**

We have financed our operations primarily from cash provided by operating activities, the sale of our common stock and the issuance of the Notes in December 2012. We have generated positive operating cash flows in each of our last 15 completed fiscal years. Accordingly, we believe that the cash generated from our operations and the cash and cash equivalents we have on hand will be sufficient to meet our operating requirements for the foreseeable future.

In addition to our operating cash requirements, we will require cash to pay interest on the Notes and to make principal payments on the Notes at maturity or upon conversion. We are permitted to settle any conversion obligation under the Notes in excess of the principal balance in either cash, shares of our common stock or a combination of cash and shares of our common stock, at our election. We intend to satisfy any conversion premium by issuing shares of our common stock. We believe that the cash generated from our operations and the cash and cash equivalents we have on hand will be sufficient to meet our future cash obligations. If our existing cash resources along with cash generated from operations is insufficient to satisfy our funding requirements we may need to sell additional equity or debt securities or seek other financing arrangements. It is our expectation that prior to December 31, 2016 we will have determined and secured our financing plans with respect to the Notes, which mature in December 2017. Although we believe based on our operations today that we will be successful in obtaining any financing necessary to satisfy the Notes upon maturity, we cannot be certain that financing alternatives will be available in amounts or at terms that are acceptable to us, or available to us at all.

One of our goals is to maintain and improve our capital structure. The key metrics we focus on in assessing the strength of our liquidity and a summary of our cash activity for the three months ended September 30, 2016 and 2015 are summarized in the tables below:

	<b>September 30, 2016</b>	<b>June 30, 2016</b>
	(in thousands)	
Cash and cash equivalents	\$ 98,706	\$ 97,174

Marketable securities	29,182	35,209
Long-term Debt <sup>(1)</sup>	173,229	169,857

- (1) Our long-term debt consists of the Notes. The Notes are shown on our Consolidated Balance Sheets at their carrying value, which represents the principal balance of \$189.8 million less unamortized discount and debt issuance costs.

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	<b>September 30,</b>	
	<b>2016</b>	<b>2015</b>
	(in thousands)	
Cash provided by operating activities	\$ 8,497	\$ 10,926
Cash used in investing activities	(4,028)	(6,830)
Cash used in financing activities	(2,380)	(19,892)
Effect of exchange rates on cash	(557)	(1,230)

*Cash, cash equivalents and marketable securities.* At September 30, 2016 our cash and cash equivalents of \$98.7 million consisted primarily of cash deposits held at major banks and money market funds. The \$1.5 million increase in cash and cash equivalents at September 30, 2016 from June 30, 2016 was primarily due to cash provided by operating activities of \$8.5 million and proceeds from the sale of available-for-sale securities of \$13.5 million, offset in part by cash of \$9.9 million used for capital expenditures, including capitalization of software costs, cash used for purchases of available-for-sale securities of \$7.6 million and cash used to repurchase shares of our common stock for an aggregate purchase price of \$3.8 million.

At September 30, 2016 our marketable securities of \$29.2 million consisted primarily of US treasury notes, residential mortgage-backed securities and US corporate debt securities.

Cash, cash equivalents and marketable securities included approximately \$44.2 million held by our foreign subsidiaries as of September 30, 2016. Our current intention is to reinvest these amounts in the growth of our foreign operations. If our reinvestment plans change based on future events and we decide to repatriate these amounts to fund our domestic operations, the amounts would generally become subject to tax in the US to the extent there were cumulative profits in the foreign subsidiary from which the distribution to the US was made.

Cash and cash equivalents held by our foreign subsidiaries are denominated in currencies other than US Dollars. Decreases in the foreign currency exchange rates of the British Pound, Swiss Franc, and Australian Dollar to the US Dollar decreased our overall cash balances by approximately \$0.6 million in the quarter ended September 30, 2016. Further changes in the foreign currency exchange rates of these currencies could have a significant effect on our overall cash balances. However, we continue to believe that our existing cash balances, even in light of the foreign currency volatility we frequently experience, are adequate to meet our operating requirements for the foreseeable future.

*Operating Activities.* Cash generated from operating activities primarily relates to our net loss less the impact of non-cash expenses and changes in working capital. Cash generated from operations decreased by \$2.4 million in the three months ended September 30, 2016 versus the same period in the prior fiscal year. In addition to the increase in our net loss for the three months ended September 30, 2016 versus the same period in the prior fiscal year of \$6.3 million, the decrease in cash generated from operations was primarily related to an increase in cash used by deferred revenue of \$4.6 million, an increase in cash used by prepaid expenses of \$0.9 million and an increase in cash used by accounts payable of \$0.4 million, offset in part by an increase in cash provided by accounts receivable of \$5.4 million, cash provided by other assets of \$1.2 million and a decrease in cash used by accrued expenses of \$1.6 million and other liabilities of \$0.8 million.

At September 30, 2016, we had US net operating loss carryforwards of \$88.9 million, which expire at various times through fiscal year 2037, Canadian net operating loss carryforwards of \$0.4 million, which expire principally in fiscal year 2035, and other foreign net operating loss carryforwards of \$12.9 million, primarily in Europe, which have no statutory expiration date. We also have approximately \$5.5 million of research and development tax credit carryforwards available which expire at various points through fiscal year 2037. Our operating losses and tax credit



carryforwards may be subject to limitations under provisions of the Internal Revenue Code.

At September 30, 2016, a portion of our deferred tax assets have been reserved since, given the available evidence, it was deemed more likely than not that these deferred tax assets would not be realized.

*Investing Activities.* The \$2.8 million decrease in net cash used in investing activities for the three months ended September 30, 2016 versus the same period in the prior fiscal year was primarily due to an increase in cash provided by proceeds from sales of available-for-sale securities of \$9.7 million partially offset by an increase in the cash used for the purchase of available-for-sale securities of \$2.8 million and an increase in the cash of \$4.1 million used for capital expenditures, including capitalization of software costs.

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*Financing Activities.* The decrease in cash used in financing activities for the three months ended September 30, 2016 as compared to the same period in the prior fiscal year was due to a decrease in cash used to repurchase our common stock of \$17.6 million.

***Contractual Obligations***

Following is a summary of future payments that we are required to make under existing contractual obligations as of September 30, 2016:

	Payment Due by Fiscal Year				Total
	2017	2018-2019	2020-2021	Thereafter	
	(in thousands)				
Long-term debt:					
Principal payment (due December 2017)	\$	\$ 189,750	\$	\$	\$ 189,750
Interest payments	2,846	1,423			4,269
Operating leases	4,011	9,535	7,549	9,314	30,409
Purchase commitments	5,366	10,426	666		16,458
Total contractual obligations	\$ 12,223	\$ 211,134	\$ 8,215	\$ 9,314	\$ 240,886

Purchase orders are not included in the table above. Our purchase orders represent authorizations to purchase rather than binding agreements. The contractual obligation amounts in the table above are associated with agreements that are enforceable and legally binding and that specify all significant terms, including: fixed or minimum services to be used; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Obligations under contract that we can cancel without a significant penalty are not included in the table above.

Our estimate of unrecognized tax benefits for which cash settlement may be required, in the amount of \$1.4 million, has been excluded from the table above. These amounts have been excluded because, as of September 30, 2016, we are unable to estimate the timing of future cash outflows, if any, associated with these liabilities as we do not currently anticipate settling any of these tax positions with cash payment in the foreseeable future.

The contractual obligations table above also excludes our estimate of the contributions we will make to our Swiss defined benefit pension plan in fiscal year 2017 which is \$1.6 million based on foreign exchange rates in effect on September 30, 2016. We are unable to estimate contribution amounts for periods after fiscal year 2017.

***Off-Balance Sheet Arrangements***

During the three months ended September 30, 2016 we did not have any off-balance sheet arrangements.

**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

We are exposed to a variety of risks, including interest rate changes, foreign currency exchange rate fluctuations, and derivative instruments classification. We have not entered into any foreign currency hedging transactions or other instruments to minimize our exposure to foreign currency exchange rate fluctuations nor do we presently plan to in the future. Also, we have not entered into any interest rate swap agreements, or other instruments to minimize our exposure to interest rate fluctuations. There has been no material change to our exposure to market risk from that

which was disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2016 as filed with the SEC on August 29, 2016, which is incorporated herein by reference.

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

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2016. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers as appropriate, to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Based on the evaluation of our disclosure controls and procedures as of September 30, 2016, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

No change in our internal control over financial reporting occurred during the fiscal quarter ended September 30, 2016 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, from time to time, a party to legal proceedings and claims that arise in the ordinary course of our business. We do not believe that there are claims or proceedings pending against us for which the ultimate resolution would have a material effect on, or require disclosure in, our financial statements.

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

*Investing in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below before making an investment decision involving our common stock. The risks and uncertainties described below are not the only ones facing us. Additional risks and uncertainties may also impact our business operations.*

*If any of the following risks actually occur, our business, financial condition or results of operations would likely suffer. In that case, the trading price of our common stock could fall, and you may lose all or part of the money you paid to buy our common stock.*

*The risk factors below do not reflect material changes from the risk factors disclosed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended June 30, 2016.*

### **Risks Related To Owning Our Common Stock**

**Our common stock has experienced and may continue to undergo significant market price fluctuations**

The market price of our common stock has recently experienced and may continue to experience significant fluctuations due to a variety of factors, including:

general and industry-specific business, economic and market conditions;

changes in or our failure to meet analysts' or investors' estimates or expectations;

actual or anticipated fluctuations in our operating results;

public announcements concerning us, our competitors or our industry;

acquisitions, divestitures, strategic partnerships, joint ventures, or capital commitments by us or our competitors;

adverse developments in patent or other proprietary rights; and

announcements of technological innovations by our competitors.

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### **If our revenues are below anticipated levels or if our operating results are below analyst or investor expectations, the market price of our common stock could be adversely affected**

A significant percentage of our expenses, particularly personnel and facilities costs, are relatively fixed and based in part on anticipated revenue levels which can be difficult to predict. A decline in revenues without a corresponding and timely slowdown in expense growth could adversely affect our business. Significant revenue shortfalls in any quarter may cause significant declines in operating results since we may be unable to reduce spending in a timely manner.

Quarterly or annual operating results that are below the expectations of public market analysts could adversely affect the market price of our common stock. Factors that could cause fluctuations in our operating results include:

a change in customer demand for our products, which is highly dependent on our ability to continue to offer innovative technology solutions in very competitive markets;

overall economic conditions, which may affect our customers' and potential customers' budgets for information technology expenditures;

foreign exchange rate volatility, which can have a significant effect on our total revenues and costs when our foreign operations are translated to US dollars;

the timing of customer orders;

the timing of product implementations, which are highly dependent on customers' resources and discretion;

the incurrence of costs relating to the integration of software products and operations in connection with acquisitions of technologies or businesses; and

the timing and market acceptance of new products or product enhancements by either us or our competitors.

### **Our mix of products and services could have a significant effect on our results of operations and the market price of our common stock**

The gross margins for our products and services vary considerably. Our software license revenues generally yield significantly higher gross margins than do our subscriptions and transactions, service and maintenance and other revenue streams. If software license revenues or our recurring revenues significantly decline in any future period, or if the mix of our products and services in any given period does not match our expectations, our results of operations and the market price of our common stock could be significantly adversely affected.

## Risks Related To Our Business

**The voting result of the Referendum of the United Kingdom's Membership of the European Union (EU) (referred to as Brexit), advising for the exit of the United Kingdom (UK) from the European Union, could cause disruptions to and create uncertainty surrounding our business, including affecting our relationships with our existing and future customers, suppliers and employees, which could have an adverse effect on our business, financial results and operations.**

As a result of the Referendum, it is expected that the British government will begin negotiations to determine the future terms of the UK's relationship with the EU, including the terms of trade between the UK and the EU. The ultimate effects of Brexit will depend on any agreements the UK makes to retain access to EU markets either during a transitional period or more permanently. The measures could potentially disrupt the markets we serve and the tax jurisdictions in which we operate, adversely change tax benefits or liabilities in these or other jurisdictions, and may cause us to lose customers, suppliers, and employees in the UK and other countries. In addition, Brexit could lead to legal uncertainty and potentially divergent national laws and regulations as the UK determines which EU laws to replace or replicate.

The announcement of Brexit caused significant volatility in global stock markets and currency exchange rate fluctuations that resulted in the strengthening of the US dollar against foreign currencies in which we conduct business, particularly the British Pound Sterling which decreased to the lowest exchange levels seen since 1985. Any strengthening of the US dollar relative to other foreign currencies affects our results of operations in a number of ways, including:

Our international sales are predominately denominated in currencies other than US dollars. A decrease of foreign currency exchanges rates will have the effect of decreasing our overall revenues upon translation to US dollars;

Any significant devaluation of foreign currencies may impact the purchasing power of our customers and potential customers and could affect the demand for our products; and

EU member countries could make it more difficult for our UK subsidiary or us to trade effectively or competitively in those regions.

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The announcement of Brexit may also create global economic uncertainty or consequences that are not yet clear given the unprecedented nature of the event.

### **The markets in which we compete are extremely competitive and we may not be able to compete effectively**

The markets in which we compete are intensely competitive and characterized by rapid technological change. There is no assurance that we will be able to maintain our current market share or our customer base.

We compete with a wide range of companies ranging from small start-up enterprises with limited resources, which we compete with principally on the basis of technology features or specific customer relationships, to large companies which can leverage significantly larger customer bases and greater financial resources. Many of our competitors have longer operating histories, significantly greater financial, technical, and sales and marketing resources, greater brand recognition and a larger customer base than we do. We anticipate that the markets in which we compete will continue to attract new competitors and new technologies and we may not be able to compete successfully with them.

To compete successfully, we need to maintain a successful research and development function. If we fail to enhance our current products and develop new, innovative solutions or if we fail to bring new solutions to market quickly enough, our products could become less competitive or obsolete.

### **We continue to make significant investments in our existing products and our new product offerings, which may adversely affect our operating results or may not be successful**

Given the highly competitive and rapidly evolving technology environment we operate within, we believe that it is important to constantly enhance our existing product offerings as well as to develop new product offerings to meet strategic opportunities as they evolve. This includes developing and enhancing our products to include what we believe is necessary to meet the future needs of our customers.

Our operating results have been affected by increases in product development expenses in recent years as we have continued to make investments in a number of our products, and as we have funded new product development based on market opportunities. We expect to continue to make these investments and we may at any time, based on product need or marketplace demand, decide to significantly increase our product development expenditures in these or other products.

Investments in existing products and new product offerings can have a negative impact on our operating results and any new product enhancement or offering may not be accepted in the marketplace or generate material revenues for us.

### **Acquisitions could disrupt our business and harm our financial condition**

An active acquisition program is an important element of our corporate strategy. We have been an acquisitive company historically, and we expect to continue to make acquisitions in the future. Any acquisition or strategic investment we have made or may make in the future may entail numerous risks, including the following:

difficulties integrating acquired operations, personnel, technologies or products;



entrance into markets and operating geographies in which we have no or limited prior experience or knowledge;

failure to realize anticipated revenue increases for any number of reasons, including if a larger than expected number of acquired customers decline to renew software maintenance contracts or subscription based contracts, if we are unsuccessful in selling the acquired products into our existing customer base or if the terms of the acquired contracts do not permit us to recognize revenue on a timely basis;

costs incurred to combine the operations of companies we acquire, such as integrations costs, transitional employee expenses and employee retention or relocation expenses may be higher than expected;

write-offs related to existing or acquired assets such as deferred tax assets, goodwill or other intangible assets;

inability to retain key personnel of the acquired company;

inadequacy of existing operating, financial and management information systems to support the combined organization, including the difficulty in integrating an acquired company's accounting, financial reporting and other administrative systems to permit effective management;

difficulties implementing controls, procedures and policies appropriate for a public company at companies that, prior to the acquisition, may have lacked such controls, policies and procedures;

in the case of foreign acquisitions, challenges integrating operations across different cultures and languages and addressing the particular regulatory, economic, currency and political risks associated with different countries or regions;

diversion of management's focus from our core business concerns;

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dilution to existing stockholders and our earnings per share;

incurrence of substantial debt;

exposure to litigation from third parties, including claims related to intellectual property or other assets acquired or liabilities assumed; and

failure to realize anticipated benefits of the transaction due to the above factors or other factors.

Any such difficulties encountered as a result of any merger, acquisition or strategic investment could have a material adverse effect on our business, operating results and financial condition.

**As a result of our acquisitions, we could be subject to significant future write-offs with respect to intangible assets, which may adversely affect our future operating results**

The carrying value of our intangible assets, including goodwill, represents a significant portion of our total assets. We periodically review our goodwill and our other intangible assets for impairment and could, in any future period, be subject to impairment charges with respect to these assets or intangible assets arising as a result of acquisitions in future periods. Any such charges, to the extent occurring, would likely have a material adverse effect on our operating results.

**The failure of our cyber fraud and risk management products to prevent a security breach or detect a cyber fraud, or the failure of our customers to take action based on the risks identified by these products could harm our reputation and adversely impact our operating results**

Our cyber fraud and risk management products provide our customers the ability to configure a multitude of settings and establish certain rule-based alerts and it is possible that a customer could misconfigure these products or fail to configure these products in an optimal manner, which could cause threats to go undetected. Similarly, if our cyber fraud and risk management products detect threats or otherwise alert a customer to suspicious activity but the customer does not take action to investigate those threats or alerts, customers may erroneously believe that our products were not effective.

Any real or perceived defects, errors or vulnerabilities in our cyber fraud and risk management products or any failure of these products to prevent, detect or alert a customer to a threat could result in:

a loss of customers or potential customers;

delayed or lost revenue and harm to our financial condition and results or operations;

a delay in attaining, or the failure to attain, market acceptance for our cyber fraud and risk management solutions;

an increase in warranty claims;

harm to our reputation;

litigation, regulatory inquiries, or investigations that may be expensive and that would further harm our reputation.

**Weakness or deterioration in domestic and global economic conditions could have a significant adverse impact on our business, financial condition and operating results**

Our business, financial condition and operating results are significantly affected by general economic conditions. The US and global economies have experienced deterioration in the recent past and prospects for sustained economic recovery remain uncertain. Prolonged economic weakness or any further downturn in the US and global economies could result in a variety of risks to our business, including:

increased volatility in our stock price;

increased volatility in foreign currency exchange rates;

delays in, or curtailment of, purchasing decisions by our customers or potential customers either as a result of continuing economic uncertainty or as a result of their inability to access the liquidity necessary to engage in purchasing initiatives;

pricing pressures for our products and services, including reductions in the duration or renewal rates for our subscription contracts and software maintenance contracts;

increased credit risk associated with our customers or potential customers, particularly those that may operate in industries or geographic regions most affected by the economic downturn; and

impairment of our goodwill or other assets.

To the extent that economic conditions remain uncertain or deteriorate, or any of the above risks occur, our business and operating results could be significantly and adversely affected.

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**We face risks associated with our international operations that could harm our financial condition and results of operations**

A significant percentage of our revenues have been generated by our international operations and our future growth rates and success are in part dependent on our continued growth and success in international markets. As is the case with most international operations, the success and profitability of these operations are subject to numerous risks and uncertainties that include, in addition to the risks our business as a whole faces, the following:

currency exchange rate fluctuations, particularly with the British Pound Sterling, the Swiss Franc, the European Euro, the Israeli Shekel and the Australian Dollar;

difficulties and costs of staffing and managing foreign operations;

differing regulatory and industry standards and certification requirements;

the complexities of tax laws in foreign jurisdictions;

the complexities of foreign data privacy laws and regulations;

the complexities of various sanctions regimes and related commercial restrictions

reduced protection for intellectual property rights in some countries; and

import or export licensing requirements.

**We are subject to the political, economic and security conditions in Israel**

We have a subsidiary headquartered in Tel Aviv, Israel. Since the establishment of the State of Israel, a number of armed conflicts have taken place between Israel and its neighbors. During the past several years, Israel has experienced periodic armed conflicts which have involved missile strikes into Israel and which at times have disrupted day-to-day civilian activity in Israel.

There can be no assurance that future attacks will not occur and that such attacks will not hit our premises or major infrastructure and transport facilities in the country, which could have an adverse effect on our ability to conduct business in Israel. In addition, acts of terrorism, armed conflicts or political instability in the region could negatively affect global as well as local economic conditions and adversely impact our operating results.

**Our business and operating results are subject to fluctuations in foreign currency exchange rates**

We conduct a substantial portion of our operations outside of the US, principally in the United Kingdom and in continental Europe and, to a lesser extent, in the Asia-Pacific and Middle East regions. During the three months ended September 30, 2016, approximately 40% of our revenues and 41% of our operating expenses were attributable to customers or operations located outside of North America. During the three months ended September 30, 2016 as compared to the three months ended September 30, the foreign currency exchange rates of the British Pound Sterling to the US Dollar decreased. Future appreciation of the US Dollar against the British Pound Sterling, Swiss Franc, European Euro or Australian Dollar will have the impact of reducing both our revenues and operating expenses associated with our operations in those regions.

**We may have larger than anticipated tax liabilities**

The determination of our provision for income taxes requires significant judgment and estimation and there are many transactions and calculations where the ultimate tax determination is uncertain. We are subject to tax in multiple US and foreign tax jurisdictions and the determination of our tax liability is always subject to audit and review by the applicable domestic or foreign taxing authority. In light of fiscal challenges in US federal and state governments and in many international locations, taxing authorities are increasingly focused on ways to increase revenues which may make resolving tax disputes more difficult. While we have established tax reserves using assumptions and estimates that we believe to be reasonable, these reserves may prove insufficient in the event that a taxing authority asserts a tax position that is contrary to our position.

**A significant percentage of our revenues to date have come from our payment and document management offerings and our future performance will depend on continued market acceptance of these solutions**

A significant percentage of our revenues to date have come from the license and maintenance of our payment and document management offerings and sales of associated products and services. Any significant reduction in demand for our payment and document management offerings could have a material adverse effect on our business, operating results and financial condition. Our future performance could depend on the following factors:

retaining and expanding our software maintenance and subscriptions and transactions customer bases, which are significant sources of our recurring revenue;

continued market acceptance of our payment and document management offerings;

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our ability to demonstrate the value of our solutions as compared to solutions from other vendors such as enterprise resource planning software vendors that offer a broader enterprise application solution; and

our ability to introduce enhancements to meet the market's evolving needs for secure payments and cash management solutions.

**Our future financial results will be affected by our success in selling our products in a subscription and transaction model, which carries with it certain risks**

A substantial portion of our revenues and profitability were historically generated from perpetual software license revenues; however, we are offering a growing number of our products, including our newer cyber fraud and risk management products, under a subscription and transaction based revenue model. We believe a subscription based revenue model has certain advantages over a perpetual license model, including better predictability of revenue; however, it also presents a number of risks to us, including the following:

arrangements entered into on a subscription basis generally delay the timing of revenue recognition and can require the incurrence of up-front costs, which may be significant;

subscription based revenue arrangements often include specific performance requirements or service levels that we may be unable to consistently achieve, subjecting us to penalties or other costs. A material breach of these arrangements by us, such as a persistent failure to achieve required service levels, might permit the customer to exit the contract prior to its expiration, without additional compensation to us;

customer retention is critical to our future growth rates. Customers in a subscription arrangement may elect not to renew their contract upon expiration, or they may attempt to renegotiate pricing or other contractual terms at the point of (or prior to) renewal on terms that are less favorable to us; and

there is no assurance that the solutions we offer on a subscription basis, including new revenue models or new products that we may introduce, will receive broad marketplace acceptance.

**Because we recognize subscription revenue from our customers over the term of their agreements, downturns or upturns in sales of our subscription based offerings will not be immediately reflected in our operating results and may adversely affect revenue in the future**

We recognize subscription revenue over the term of our customer agreements. As a result, most of our subscription revenue arises from agreements entered into during previous periods. A shortfall in orders for our subscription based solutions in any one period would most likely not significantly reduce our subscription revenue for that period, but could adversely affect revenue in future periods. In addition, we may be unable to quickly reduce our cost structure in response to a decrease in these orders. Accordingly, the effect of downturns in sales of our subscription based solutions will not be fully reflected in our operating results until future periods. A subscription revenue model also makes it difficult for us to rapidly increase our revenue through additional subscription sales in any one period, as revenue is generally recognized over the applicable customer term.

**Large and complex customer contracts, or contracts that involve the delivery of services over contractually committed periods, can delay the timing of our revenue recognition and, in the short-term, may adversely affect our operating results, financial condition and the market price of our stock**

Large and complex customer contracts can delay the timing of our revenue recognition. These arrangements require significant implementation work, product customization and modification, systems integration and user acceptance testing. This results in the recognition of revenue over the period of project completion which normally spans several quarters. Delays in revenue recognition on these contracts, including delays that result from customer decisions to halt or slow down a long-term project due to their own staffing or other challenges, could adversely affect our operating results, financial condition and the market price of our common stock. Large customer opportunities are very competitive and take significant time and effort to consummate. When competing for these customer opportunities, we face greater sales costs, longer sales cycles and less predictability with respect to these orders than with orders in other areas of our business. If we are unable to continue to generate new large orders on a regular basis, our business operating results and financial condition could be adversely affected.

**If our products and services do not comply with laws, regulations and industry standards to which we and our customers are subject, our business could be adversely affected**

Our software products and SaaS offerings facilitate the transmission of cash, business documents and confidential information including, in some cases, personally identifiable information related to individuals and corporations. Our software products and certain of our SaaS offerings store and transmit this data electronically, and therefore our products must operate within the laws, regulations and industry standards regarding security, data protection and electronic commerce. While we believe that our products comply with

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current regulatory requirements, the interpretation and application of these requirements continues to evolve and may evolve in ways that we cannot predict; so there can be no assurance that future legal or regulatory actions will not adversely impact us. To the extent that current or future regulatory or legal developments mandate a change in any of our products or services, require us or our customers to comply with any industry specific licensing or compliance requirements, alter the demand for or the competitive environment of our products and services or require us to make material changes to how we operate our business, including any changes to our internal operating, financial or management information systems, we might not be able to respond to such requirements in a timely or cost effective manner. If this were to occur, our business, operating results and financial condition could be materially adversely affected.

### **Security or data breaches could have an adverse effect on our business**

In the course of providing services to our customers, we collect, store, process and transmit highly sensitive and confidential information. Certain of our solutions also facilitate the actual transfer of cash or transmit instructions that initiate cash transfer. Our products and services, particularly our SaaS and Web-based offerings, may be vulnerable to unauthorized access, computer viruses, cyber-attacks, distributed denial of service attacks and other disruptive problems which could result in the theft, destruction or misappropriation of confidential information. Security risks in recent years have increased significantly given the increased sophistication and activities of hackers, organized crime and other external parties. We may need to spend significant capital or allocate significant resources to ensure effective ongoing protection against the threat of security breaches or to address security related concerns. Despite our efforts, a security breach or computer virus could still occur which could have a significant negative impact on our business, including reputational harm, the loss of customers and material financial liability to us.

### **Defects or disruptions in our products or services could diminish demand for our solutions and have a material adverse effect on our future financial results**

Our software products are complex. Despite testing prior to their release and throughout the lifecycle of a product or service, software and SaaS offerings can contain undetected errors or defects that can impact their function, performance and security. Any unanticipated performance problems or defects in our products or services could result in additional development costs, diversion of technical and other resources from our other development efforts, service disruptions for our SaaS offerings, negative publicity and reputational harm to us and our products and exposure to potential liability claims. As a result, any error or defect in our products or services could adversely affect our future financial results.

### **We rely on certain third-party hardware and software which could cause errors, interruptions or failures to our solutions or be difficult to replace**

We rely on third party hardware and software to deliver certain of our solutions. These third party products may not continue to be available to us on commercially reasonable terms, or at all. The loss of the right to use any of these products could result in delays in our ability to provide our solutions until equivalent technology is either developed by us or acquired from another third party, if available, which may not be possible on a cost effective basis. In addition, errors or defects in third-party products used in conjunction with our solutions could adversely affect the operation of our products.

### **Catastrophic events may disrupt our business, including our third party data centers**

We are a highly automated business and we rely on our network infrastructure, various software applications and many internal technology systems and data networks for our customer support, development, sales and marketing and



accounting and finance functions. Further, our SaaS offerings provide services to our customers from third party data center facilities in different US and international locations over which we have no control. A disruption or failure of these systems or data centers in the event of a natural disaster, telecommunications failure, power outage, cyber-attack, war, terrorist attack, or other catastrophic event could cause system interruptions, reputational harm, delays in product development, breaches of data security and loss of critical data. Such an event could also prevent us from fulfilling customer orders or maintaining certain service level requirements, particularly in respect of our SaaS and hosted offerings. While we have developed certain disaster recovery plans and maintain backup systems to reduce the potentially adverse effect of such events, a catastrophic event that resulted in the destruction or disruption of any of our data centers or our critical business or information technology systems could severely affect our ability to conduct normal business operations and, as a result, our business, operating results and financial condition could be adversely affected.

**We could incur substantial costs resulting from warranty claims or product liability claims**

Our product agreements typically contain provisions that afford customers a degree of warranty protection in the event that our products fail to conform to written specifications. These agreements normally contain provisions intended to limit the nature and extent of our risk of warranty and product liability claims. A court, however, might interpret these terms in a limited way or conclude that part or all of these terms are unenforceable. Furthermore, some of our agreements are governed by non-US law and there is a risk that foreign law might provide us less or different protection. While we maintain general liability insurance, including coverage for errors and omissions, we cannot be sure that our existing coverage will continue to be available on reasonable terms or will be available in amounts sufficient to cover one or more large claims.

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Although we have not experienced any material warranty or product liability claims to date, a warranty or product liability claim, whether or not meritorious, could harm our reputation, result in substantial financial costs or divert management's attention, which could have an adverse effect on our business, operating results and financial condition.

### **We could be adversely affected if we are unable to protect our proprietary technology and could be subject to litigation regarding intellectual property rights, which could cause serious harm to our business**

We rely upon a combination of patent, copyright and trademark laws and non-disclosure and other intellectual property contractual arrangements to protect our proprietary rights. However, there is no assurance that our patents, pending applications for patents that may issue in the future, or other intellectual property will be of sufficient scope and strength to provide meaningful protection for our technology or any commercial advantage to us. Further, we cannot be certain that our patents will not be challenged, invalidated or circumvented. We enter into agreements with our employees and customers that seek to limit and protect the distribution of proprietary information. Despite our efforts to safeguard and maintain our proprietary rights, there is no assurance that such rights will remain protected or that we will be able to detect unauthorized use and take appropriate steps to enforce our intellectual property rights.

Litigation involving patents and other intellectual property rights is common in the United States and in other countries where we operate. We may be a party to litigation in the future to protect our intellectual property rights or as a result of an alleged infringement of the intellectual property rights of others. Any such claims, whether or not meritorious, could result in reputational harm to us, require us to spend significant sums in litigation costs or damages, delay product implementations, or require us to develop non-infringing intellectual property or acquire licenses to intellectual property that is the subject of the infringement claim. In addition, under many of our customer contracts, we are required to indemnify our customers for third-party intellectual property infringement claims, which would increase the costs to us of any such claims. These claims could have a material adverse effect on our business, operating results and financial condition.

### **Our ability to attract and retain qualified employees is critical to the success of our business and failure to do so could adversely affect our operating results**

Our success depends upon the efforts and abilities of our executive officers and technical and sales employees who are skilled in e-commerce, payment methodology and regulation, business banking technologies, and web, database and network technologies. Our success and future growth depends to a significant degree on the skills and continued services of our management team. Our current key employees and employees whom we seek to hire in order to support our growth are in high demand within the marketplace and many competitors, customers and industry organizations are able to offer considerably higher compensation packages than we currently provide, including base salary, bonus and equity incentives. The loss of one or more of our key employees or our failure to consistently attract and retain sufficient qualified employees to grow our operations could have a material adverse effect on our business. We do not maintain key man life insurance policies on any of our employees and our employees are generally free to terminate their employment with us at any time. The loss of the services of any of our executive officers or other key employees could have a material adverse effect on our business, operating results and financial condition.

### **We engage off-shore development resources which may not be successful and which may put our intellectual property at risk**

In order to optimize our research and development capabilities and to meet development timeframes, we contract with off-shore third-party vendors for certain development activities. While our experience to date with these resources has been positive, there are a number of risks associated with off-shore development activities including:

less efficient and less accurate communication and information flow as a consequence of time, distance and language barriers between our primary development organization and the off-shore resources, resulting in delays or deficiencies in development efforts;

disruption due to political or military conflicts;

misappropriation of intellectual property, which we may not readily detect; and

currency exchange rate fluctuations that could adversely impact the cost advantages intended from these agreements.

To the extent that these or unforeseen risks occur, our operating results and financial condition could be adversely impacted.

**Changes in financial accounting standards may cause unexpected financial reporting fluctuations and affect our reported results of operations**

Changes in accounting standards or practices could adversely affect our reported results of operations. New accounting pronouncements, such as the upcoming changes in US GAAP related to revenue recognition, accounting for lease arrangements and

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accounting for share-based compensation arrangements, and varying interpretations of accounting pronouncements, have occurred and will occur in the future. Changes to existing accounting rules or practices may adversely affect our reported results of operations or the way we conduct our business in future periods.

### **If we fail to maintain appropriate and effective internal control over financial reporting, our ability to produce accurate and timely financial statements could be impaired, which could result in a loss of investor confidence in our financial reports and have an adverse effect on our stock price**

Ensuring that we have adequate internal financial and accounting controls and procedures in place so that we can produce accurate financial statements on a timely basis is a costly and time-consuming effort that we re-evaluate regularly. Our internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with GAAP. However, despite our efforts, any failure to maintain or implement the necessary internal controls could cause us to fail to meet our financial reporting obligations or result in misstatements in our financial statements, either of which could cause investors to lose confidence in our reported financial information and lead to a decline in the trading price of our common stock.

### **Certain anti-takeover provisions contained in our charter and under Delaware law could hinder a takeover attempt**

We are subject to the provisions of Section 203 of the General Corporation Law of the State of Delaware prohibiting, under some circumstances, publicly-held Delaware corporations from engaging in business combinations with some stockholders for a specified period of time without the approval of the holders of substantially all of our outstanding voting stock. Such provisions could delay or impede the removal of incumbent directors and could make more difficult a merger, tender offer or proxy contest involving us, even if such events could be beneficial, in the short term, to the interests of our stockholders. In addition, such provisions could limit the price that some investors might be willing to pay in the future for shares of our common stock. Our certificate of incorporation and bylaws contain provisions relating to the limitation of liability and indemnification of our directors and officers, dividing our board of directors into three classes of directors serving three-year terms and providing that our stockholders can take action only at a duly called annual or special meeting of stockholders.

### **Risks Related to our Indebtedness**

In December 2012, we issued, at par value, \$189.8 million aggregate principal amount of 1.50% convertible senior notes due in December 2017. In connection with the pricing of the notes, we purchased convertible note hedge transactions with a strike price equal to the initial conversion price of the notes and we sold warrants with a strike price of \$40.04 per share with certain counterparties. The note hedges and the warrants each cover approximately 6.3 million shares of our common stock.

### **Servicing the notes or future indebtedness will require a significant amount of cash, and we may not have sufficient cash flow from our business to pay our obligations under the notes or future indebtedness, resulting in a default under such indebtedness**

Our ability to make scheduled payments of interest and, upon maturity or early conversion, the principal balance of the notes, depends on our future performance which is subject to economic, financial, competitive and other factors beyond our control. Our business may not continue to generate cash flow from operations in the future sufficient to service our debt. If we are unable to generate such cash flow, we may be required to adopt one or more alternatives, such as selling assets, restructuring debt or obtaining additional debt or equity financing on terms that may not be

favorable to us or available to us at all. Our ability to refinance the notes will depend on the capital markets and our financial condition at that time. We may not be able to engage in any of these activities or engage in these activities on desirable terms, which could result in a default on the notes or future indebtedness.

**Our level of indebtedness may limit our financial flexibility**

Our level of indebtedness affects our operations in several ways, including:

a portion of our cash flows from operating activities must be used to service our indebtedness and is not available for other purposes;

we may be at a competitive disadvantage as compared to similar companies that have less debt; and

additional financing in the future for working capital, capital expenditures, acquisitions, general corporate or other purposes may have higher costs and contain restrictive covenants, or may not be available to us. The factors that will affect our ability to obtain additional financing may be beyond our control and include financial market conditions, the value of our assets and our performance at the time we need financing.

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### **The accounting for the notes will result in our having to recognize interest expense significantly more than the stated interest rate of the notes and may result in volatility to our consolidated statement of operations**

Upon issuance of the notes we were required to establish a separate initial value for the conversion option and to bifurcate this value from the value attributable to the balance of the notes, or the debt component. As a result, for accounting purposes, we were required to treat the notes as having been issued with a discount to their face principal amount, which is referred to as an original issue discount. We are accreting the original issue discount to interest expense ratably over the term of the notes, which results in an effective interest rate in our consolidated statement of operations that is in excess of the stated coupon rate of the notes. This will reduce our earnings and could adversely affect the price at which our common stock trades, but will have no effect on the amount of cash interest paid to holders or on our cash flows.

Certain derivative instruments issued in connection with the notes were classified within stockholders' equity at September 30, 2016. However, if we do not continue to satisfy all of the criteria required for equity classification, these instruments would be reclassified out of equity and be subject to re-measurement at fair value. Changes in fair value resulting from any such re-measurement would be reflected in earnings which could have a material impact on our financial statements.

### **The conditional conversion feature of the notes, if triggered, and the requirement to repurchase the notes upon a fundamental change may adversely affect our financial condition and operating results**

In the event the conditional conversion feature of the notes is triggered, holders of notes will be entitled to convert the notes at their option during specified periods. If one or more holders elect to convert their notes, we would be required to settle the principal portion of the notes in cash. Additionally, if we undergo a fundamental change, (as described in the Indenture), subject to certain conditions, holders of the notes may require us to repurchase for cash all or part of their notes at a price equal to 100% of the principal amount of the notes, plus accrued and unpaid interest. Either of these events could adversely affect our liquidity. Even if holders do not elect to convert their notes, we could be required under applicable accounting rules to reclassify all or a portion of the outstanding principal balance of the notes to a current rather than long-term liability, which would result in a material reduction of our working capital.

### **We may be subject to significant future write-offs with respect to intangible assets or deferred tax assets**

Certain of our assets, such as intangible assets and deferred tax assets, are subject to periodic tests of recoverability based on a variety of factors. Those factors typically include, at a minimum, projections of future income levels and cash flows. The accounting for the notes will result in the recognition of a significant level of interest expense as the carrying value of debt is accreted to par value and as we amortize our debt issue costs, including the underwriters discount. We could be subject to future impairment charges with respect to these assets which would have a material adverse effect on our consolidated statement of operations.

### **The convertible note hedge and warrant transactions may affect the value of the notes and our common stock**

The outstanding warrants could have a dilutive effect on our earnings per share to the extent that the market price per share of our common stock exceeds the applicable strike price of the warrants. However, subject to certain conditions, we may elect to settle the warrants in cash.

From time to time, the counterparties to the convertible note hedge transactions or their affiliates may modify their respective hedge positions by entering into or unwinding various derivatives with respect to our common stock and/or purchasing or selling our common stock or other securities of ours in secondary market transactions (and are likely to

do so during any observation period related to a conversion of notes). This activity could cause or avoid an increase or a decrease in the market price of our common stock or the notes.

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

The following table provides information about purchases by us of our common stock during the quarter ended September 30, 2016:

<b>Period</b>	<b>Total Number of Shares Purchased(1)</b>	<b>Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs</b>
July 1, 2016 - July 31, 2016				
August 1, 2016 - August 31, 2016				\$
September 1, 2016 - September 30, 2016	214,111	\$ 23.21	214,111	\$ 55,030,484
<b>Total</b>	<b>214,111</b>		<b>214,111</b>	<b>\$ 55,030,484</b>

- (1) On July 8, 2016 our board of directors authorized a repurchase program of our common stock for an aggregate repurchase price not to exceed \$60 million. This program expires on July 8, 2018.

**Item 6. Exhibits**

See the Exhibit Index for a list of exhibits filed as part of this Quarterly Report on Form 10-Q, which Exhibit Index is incorporated herein by reference.



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**SIGNATURE**

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.

**Bottomline Technologies (de), Inc.**

Date: November 8, 2016

By: /s/ RICHARD D. BOOTH  
**Richard D. Booth**  
**Chief Financial Officer and Treasurer**  
**(Principal Financial and Accounting Officer)**

**Table of Contents****EXHIBIT INDEX**

<b>Exhibit Number</b>	<b>Description</b>	<b>Incorporate by Reference</b>			<b>Filed Herewith</b>
		<b>Form</b>	<b>File No.</b>	<b>Exhibit</b>	
10.1	Amendment No. 4 to 2009 Stock Incentive Plan				X
10.2	Executive Retention Agreement dated as of August 5, 2016 between the Registrant and John F. Kelly	8-K	000-25259	10.1	8/5/2016
31.1	Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer				X
31.2	Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer				X
32.1	Section 1350 Certification of Principal Executive Officer				X
32.2	Section 1350 Certification of Principal Financial Officer				X
101.INS**	XBRL Instance Document				X
101.SCH**	XBRL Taxonomy Extension Schema Document				X
101.CAL**	XBRL Taxonomy Calculation Linkbase Document				X
101.DEF**	XBRL Taxonomy Definition Linkbase Document				X
101.LAB**	XBRL Taxonomy Label Linkbase Document				X
101.PRE**	XBRL Taxonomy Presentation Linkbase Document				X

\*\* submitted electronically herewith

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets as of September 30, 2016 (unaudited) and June 30, 2016, (ii) Unaudited Condensed Consolidated Statements of Comprehensive Loss for the three months ended September 30, 2016 and 2015, (iii) Unaudited Condensed Consolidated Statements of Cash Flows for the three months ended September 30, 2016 and 2015 and (iv) Notes to Unaudited Condensed Consolidated Financial Statements.

