GAIAM INC
Form PRE 14A
May 26, 2006

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

# SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of
the Securities Exchange Act of 1934 (Amendment No. )

Filed by the Registrant ý

Filed by a Party other than the Registrant o

Check the appropriate box:

| | |
|---|---|
| ý | Preliminary Proxy Statement |
| o | **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))** |
| o | Definitive Proxy Statement |
| o | Definitive Additional Materials |
| o | Soliciting Material Pursuant to §240.14a-12 |

**Gaiam, Inc.**
(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

ý No fee required.

o Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

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| (1) | Title of each class of securities to which transaction applies: |
| (2) | Aggregate number of securities to which transaction applies: |
| (3) | Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined): |
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o Fee paid previously with preliminary materials.

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| | |
|---|---|
| (1) | Amount Previously Paid: |
| (2) | Form, Schedule or Registration Statement No.: |
| (3) | Filing Party: |
| (4) | Date Filed: |

**Gaiam, Inc.**
**360 Interlocken Boulevard**
**Broomfield, Colorado 80021**

**NOTICE OF SPECIAL MEETING OF SHAREHOLDERS**
**TO BE HELD ON THURSDAY, JUNE 22, 2006**

To Our Shareholders:

A special meeting of shareholders of Gaiam, Inc., a Colorado corporation, will be held on Thursday, June 22, 2006, at 9:30 a.m. at Hotel Boulderado, 2115 13th Street, Boulder, Colorado 80302. This meeting has been called to amend Gaiam s Articles of Incorporation to allow certain shareholder actions in accordance with changes made in the Colorado Business Act, more specifically:

1. to authorize an amendment to our Articles of Incorporation to provide that any action of shareholders that would otherwise require a shareholders meeting may be taken by the written consent of the required minimum number of shareholders without a meeting; and

2. to transact such other business as may properly come before the meeting, or any adjournment(s) or postponement(s) thereof.

Gaiam s board of directors has fixed the close of business on Tuesday, April 25, 2006, as the record date for determining the shareholders entitled to notice of, and to vote at, the special meeting. A complete list of shareholders entitled to vote at the meeting will be available for inspection by any shareholder of Gaiam prior to the meeting, upon written request showing a proper purpose, during normal business hours at Gaiam s Broomfield, Colorado office. Only shareholders of record on the April 25, 2006 record date are entitled to notice of, and to vote at, the special meeting and any adjournments or postponements thereof.

A Notice of Special Meeting and a proxy card accompany this notice. To ensure that your shares are represented at the meeting, we urge you to mark your choice on the enclosed proxy card, sign and date the card and return it promptly in the envelope provided. Shareholders are cordially invited to attend the special meeting in person.

By Order of the Board of Directors,

Lynn Powers, Secretary
Broomfield, Colorado
June 5, 2006

**YOUR VOTE IS IMPORTANT. WE URGE YOU TO DATE, SIGN AND PROMPTLY RETURN YOUR PROXY SO THAT YOUR SHARES MAY BE VOTED IN ACCORDANCE WITH YOUR WISHES.**

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**Gaiam, Inc.**
**360 Interlocken Boulevard**
**Broomfield, Colorado 80021**

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**PROXY STATEMENT**

**SPECIAL MEETING OF SHAREHOLDERS**
**TO BE HELD ON JUNE 22, 2006**

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This proxy statement and the accompanying proxy card are being furnished to the shareholders of Gaiam, Inc. in connection with the solicitation of proxies by and on behalf of the Board of Directors of Gaiam for use at its special meeting of shareholders to be held on Thursday, June 22, 2006, starting at 9:30 a.m. at Hotel Boulderado, 2115 13th Street, Boulder, Colorado 80302, and at any adjournment(s) or postponement(s) thereof.

**PURPOSE OF SPECIAL MEETING**

At the special meeting, shareholders will be asked: (i) to authorize an amendment to our Articles of Incorporation to provide that any action of shareholders that would otherwise require a shareholders meeting may be taken by the written consent of the required minimum number of shareholders without a meeting; and (ii) to transact such other business as may properly be brought before the meeting. Our Board recommends a vote FOR the proposal listed herein.

**QUORUM AND VOTING RIGHTS**

The presence, in person or by proxy, of the holders of a majority of the outstanding votes eligible to be cast by our Class A and Class B Common Stock is necessary to constitute a quorum at the special meeting. Only shareholders of record at the close of business on the record date, Tuesday, April 25, 2006, will be entitled to notice of, and to vote at, the special meeting. As of the record date, there were 15,358,378 shares of Class A Common Stock, par value $.0001, and 5,400,000 shares of Class B Common Stock, par value $.0001, outstanding and entitled

to vote. Holders of Class A Common Stock as of the record date are entitled to one vote for each share held and holders of Class B Common Stock as of the record date are entitled to ten votes for each share held. The holders of the Class A and Class B Common Stock will vote together. Once a quorum is present, action on a matter will be approved if the votes cast favoring the proposal exceed the votes cast opposing the proposal.

Mr. Jirka Rysavy, our Chairman and Chief Executive Officer, holds all 5,400,000 outstanding shares of Class B Common Stock and 1,664,000 shares of Class A Common Stock (or approximately 11% of the outstanding shares of Class A Common Stock). These shares are sufficient to constitute a quorum and to approve the proposal, and Mr. Rysavy has indicated that he plans to be present at the meeting and vote in favor of the proposal.

All shares of Common Stock represented by properly executed proxies will, unless the proxies have previously been revoked, be voted in accordance with the instructions indicated in the proxies. Abstentions and broker non-votes will have no effect on the result of the vote, although they will count towards the presence of a quorum. Any shareholder executing a proxy has the power to revoke the proxy at any time prior to its exercise. A proxy may be revoked prior to exercise by (a) filing with Gaiam a written revocation of the proxy, (b) appearing at the special meeting and voting in person, or (c) submitting to Gaiam a duly executed proxy bearing a later date.

The cost of preparing, printing, assembling and mailing this Proxy Statement and other material furnished to shareholders in connection with the solicitation of proxies will be borne by Gaiam. In addition, officers, directors and regular employees of Gaiam may solicit proxies by written communication, telephone or telegraph. These persons will receive no special compensation for any solicitation activities.

**IT IS THE INTENTION OF THE AGENTS DESIGNATED IN THE ENCLOSED PROXY CARD TO VOTE FOR THE PROPOSAL BELOW. JIRKA RYSAVY, WHO HOLDS APPROXIMATELY 11% OF THE OUTSTANDING SHARES OF CLASS A COMMON STOCK AND 100% OF THE OUTSTANDING SHARES OF CLASS B COMMON STOCK, HAS INFORMED GAIAM THAT HE INTENDS TO VOTE HIS SHARES IN FAVOR OF THE PROPOSAL SET FORTH IN THIS PROXY STATEMENT.**

## PROPOSAL AMENDMENT TO ARTICLES OF INCORPORATION

Effective April 22, 2005, the Colorado Business Corporation Act (the CBCA ) was amended to provide that a required minimum number of shareholders could take actions without a meeting under certain circumstances. Under Section 7-107-104 of the CBCA, as amended, if expressly permitted by the articles of incorporation of a company, the shareholders holding the required number of shares may consent to an action in writing without the need to hold a meeting. The shareholders signing the consent must have the minimum number of votes that would be necessary to authorize or take action at a meeting at which all of the shares entitled to vote thereon were present and voted.

A majority of states in which public companies are organized include similar provisions permitting action by less than unanimous written consent of shareholders. The purpose of these provisions is to streamline the corporate governance process and eliminate the need to incur the unnecessary expense associated with convening special meetings of shareholders.

Gaiam s Articles of Incorporation currently do not allow for action by written consent of shareholders entitled to vote on matters requiring their approval. Gaiam s Board of Directors has adopted a resolution, subject to shareholder approval, to amend our Articles of Incorporation to provide that shareholders holding shares having not less than the minimum number of votes that would be necessary to authorize or take action at a meeting at which all of the shares entitled to vote thereon were present and voted may consent to such action in writing as permitted by Section 7-107-104 of the CBCA, as amended.

If the proposed amendment is approved by Gaiam s shareholders, Article IV, Section F of Gaiam s Articles of Incorporation would read as follows, with the addition of the second sentence quoted below:

**F. Quorum and Voting Requirements.** At all meetings of the shareholders, the holders of a majority of the votes eligible to be cast shall constitute a quorum. If a quorum is present, the affirmative vote of a majority of the votes

eligible to be cast on the subject matter shall be the act of the shareholders unless the vote of a greater number or voting by groups is required by the Colorado Business Corporation Act or these Articles. Any action required or permitted by Articles 101 to 117 of the Colorado Business Corporation Act to be taken at a shareholders meeting may be taken without a meeting if shareholders holding shares having not less than the minimum number of votes that would be necessary to authorize or take such action at

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a meeting at which all of the shares entitled to vote thereon were present and voted consent to such action in writing.

Any solicitation to obtain written consents of the shareholders under the new provision would be required to comply with the proxy solicitation requirements of the Securities Exchange Act of 1934 and the related regulations of the SEC. In addition, the Exchange Act and related regulations would require that an information statement describing the action to be taken and explaining the reasons for such action, as well as its consequences, be sent to shareholders at least twenty (20) calendar days prior to the earliest date on which the action may be taken. Finally, Colorado law further requires that prompt written notice of any action taken by written consent of the shareholders shall be sent to those stockholders that have not given their written consent and who otherwise would have been entitled to vote on the action.

The Board believes that permitting action by less than unanimous written consent of shareholders will streamline the corporate governance process by eliminating unnecessary costs and delays associated with holding special shareholders meetings and by eliminating the expense and delays associated with obtaining unanimous written consent. The Board believes that adoption of the proposed amendment is in the best interest of Gaiam and its shareholders.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE PROPOSAL TO APPROVE THE AMENDMENT TO THE ARTICLES OF INCORPORATION**

## BENEFICIAL OWNERSHIP OF SHARES

The following table sets forth certain information with respect to the beneficial ownership of our common stock as of April 28, 2006, except as noted, for (i) each person (or group of affiliated persons) who, insofar as Gaiam has been able to ascertain, beneficially owned more than 5% of the outstanding shares of Class A or Class B Common Stock of Gaiam, (ii) each director and nominee for director, (iii) each executive officer named in the table above, and (iv) all current directors and executive officers as a group.

| Title of Class of Common Stock | Name and Address of Beneficial Owner(1) | | Amount and Nature of Beneficial Ownership(2) | Percent of Class |
|---|---|---|---|---|
| Class A | Jirka Rysavy | (3) | 7,064,000 | 34.03% |
| | Prentice Capital Management, LP | (4) | 3,338,519 | 21.74% |
| | Revolution Living LLC | (5) | 2,500,000 | 16.28% |
| | Columbia Wanger Asset Management, L.P. | (6) | 1,212,000 | 7.89% |
| | Lynn Powers | (7) | 383,000 | 2.45% |
| | James Argyropoulos | (7)(8) | 237,491 | 1.55% |
| | Janet Mathews | (7) | 42,200 | * |
| | Barnet Feinblum | (7)(9) | 31,717 | * |
| | Barbara Mowry | (7) | 22,833 | * |
| | Paul Ray | (7) | 16,121 | * |
| | Ted Nark | (7) | 5,247 | * |
| | David Golden | (5) | | |
| | All directors and officers as a group (10 persons) | (3)(7) | 7,807,609 | 36.94% |
| Class B | Jirka Rysavy | | 5,400,000 | 100.0% |
| | All directors and officers as a group (10 persons) | | 5,400,000 | 100.0% |

* Indicates less than one percent ownership

(1) The address of all persons listed is 360 Interlocken Blvd., Broomfield, Colorado, 80021, except as otherwise noted.

(2) This table is based upon information supplied by officers, directors and principal shareholders on Schedule 13Ds and 13Gs and Forms 3, 4 and 5 filed with the Securities and Exchange Commission. All beneficial ownership is direct, except as otherwise noted. Share amounts include stock options exercisable within 60 days of April 28, 2006.

(3) Includes 5,400,000 shares of Class A Common Stock obtainable upon conversion of Class B Common Stock.

(4) Based on a Schedule 13D/A filed as of May 3, 2006. Includes shares managed by Prentice Capital Management, LP and Michael Zimmerman. The address for Prentice Capital Management, LP is 623 Fifth Avenue, 32rd Floor, New York, New York 10022.

(5) Based on a Schedule 13D filed as of August 15, 2005. The address for Revolution Living LLC is 1717 Rhode Island Avenue, N.W., Washington, DC 20036. Revolution, LLC, the Stephen M. Case Revocable Trust and Stephen M. Case may be deemed to beneficially own such shares. David Golden is Executive Vice President and Chief Financial Officer of Revolution, LLC.

(6) Based on a Schedule 13G filed as of February 14, 2006. The address for Columbia Wanger Asset Management, L.P. is 227 West Monroe Street, Suite 3000, Chicago, Illinois 60606.

(7) Includes the following shares issuable upon the exercise of stock options which can be exercised within sixty days of April 28, 2006: Ms. Powers, 284,000; Mr. Argyropoulos, 10,000; Ms. Mathews, 41,600; Mr. Feinblum, 10,000; Ms. Mowry, 10,000; Mr. Nark, 5,000 and Mr. Ray, 10,000.

(8) Includes 220,000 shares of Class A Common Stock held by Argyropoulos Investors.

(9) Includes 4,000 shares of Class A Common Stock held by Mr. Feinblum s wife, as to which Mr. Feinblum disclaims beneficial ownership.

**SHAREHOLDER PROPOSALS**

Shareholders may submit proposals on matters appropriate for shareholder action at Gaiam s annual meetings consistent with regulations adopted by the Securities and Exchange Commission. For shareholder proposals to be considered for inclusion in Gaiam s proxy statement and form of proxy relating to the 2007 annual meeting of shareholders, they must be received by Gaiam not later than January 31, 2007, unless the date of the 2007 meeting of shareholders is changed by more than 30 days from June 22, 2007.

In addition, under the terms of Gaiam s Bylaws, unless the date of the 2007 meeting of shareholders is changed by more than 30 days from June 22, 2007, shareholders who intend to present an item of business or nomination at the 2007 annual meeting of shareholders (other than a proposal submitted for inclusion in Gaiam s proxy material(s)) must provide notice in writing of such business or nomination to Gaiam no earlier than March 16, 2007 and no later than April 20, 2007.

Such written notice must contain specified information, including, among other things, information as would be required to be included in a proxy statement under Securities and Exchange Commission rules, as set forth more fully in our Bylaws. All proposals or other notices should be addressed to Gaiam at 360 Interlocken Boulevard, Broomfield, Colorado 80021, Attention: Secretary.

**OTHER MATTERS**

Management does not intend to present, and has no information as of the date of preparation of this proxy statement that others will present, any business at the special meeting, other than business

pertaining to matters set forth in the special meeting and this proxy statement. However, if other matters requiring the vote of the shareholders properly come before the special meeting, it is the intention of the persons named in the enclosed proxy to vote the proxies held by them in accordance with their best judgment on such matters.

**YOUR VOTE IS IMPORTANT**

**WE URGE YOU TO DATE, SIGN AND PROMPTLY RETURN YOUR PROXY SO THAT YOUR SHARES MAY BE VOTED IN ACCORDANCE WITH YOUR WISHES AND THE PRESENCE OF A QUORUM MAY BE ASSURED.**

**GAIAM, INC.**
Proxy for Special Meeting of Shareholders
June 22, 2006

**THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS OF GAIAM, INC.**

The undersigned hereby appoints Jirka Rysavy and Lynn Powers as Proxies, each with the power to appoint his or her substitute, and hereby authorizes them to represent and to vote, as designated below, all the shares of Class A Common Stock of Gaiam, Inc. held of record by the undersigned on April 25, 2006, at the special meeting of shareholders of Gaiam, Inc. and any adjournment or postponement thereof, as follows:

The undersigned has received the Notice of Meeting, the proxy statement relating to the special meeting of shareholders to be held June 22, 2006, and hereby ratifies and confirms all that the Proxies shall lawfully do or cause to be done by virtue hereof and hereby revokes all proxies heretofore given to vote such shares.

THIS PROXY, WHEN PROPERLY EXECUTED, WILL BE VOTED AS DIRECTED HEREIN BY THE UNDERSIGNED SHAREHOLDER. **IF NO DIRECTION IS INDICATED, THIS PROXY WILL BE VOTED FOR THE PROPOSAL TO AMEND GAIAM S ARTICLES OF INCORPORATION**.

PLEASE SIGN AND RETURN PROMPTLY.

**PROPOSAL AMENDMENT TO ARTICLES OF INCORPORATION**

To authorize an amendment to our Articles of Incorporation regarding shareholder action by written consent. The Board of Directors recommends a vote FOR this proposal.

o FOR o AGAINST o ABSTAIN

In their discretion, the Proxies are authorized to vote upon such other matters as may properly come before the meeting. Management is not presently aware of any such matters to be presented for action.

Dated: , 2006

Signature 1 Signature 2

Please sign exactly as your name or names appear on this proxy. When shares are held by joint tenants, both should sign. When signing as executor, administrator, attorney, trustee or guardian, please give full title as such, and where more than one executor, etc., is named, a majority must sign. If a corporation, please sign full corporate name by president or other authorized officer. If a partnership, please sign full partnership name by an authorized person.

o Mark this box with an X if you have made changes to your name or address details.

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rtical-align:bottom;background-color:#cceeff;padding-top:2px;padding-bottom:2px;">
2,676

$
2,793

$
(946
)
(35.4
)%

$
(117
)
(4.2
)%
As a % of product revenue
5.2
%

8.3
%

13.4
%

As a % of total revenue
0.6
%

1.1
%

1.3
%

Cost of product revenue decreased for the year ended December 31, 2018 as compared to the year ended December 31, 2017, and for the year ended December 31, 2017, as compared to the year ended December 31, 2016, primarily due to a decrease in hardware sales.

Amortization of intangible assets

| | Years Ended December 31, | | | 2018 Versus 2017 | | 2017 Versus 2016 | |
|---|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | Amount | % | Amount | % |
| | (in thousands, except percentage data) | | | | | | |
| Amortization of intangible assets | $ 15,629 | $ 8,179 | $ 2,632 | $7,450 | 91.1 % | $5,547 | 210.8 % |
| As a % of total revenue | 5.3 % | 3.5 % | 1.3 % | | | | |

Amortization of intangible assets increased for the year ended December 31, 2018 as compared to the year ended December 31, 2017, and the year ended December 31, 2017, as compared to the year ended December 31, 2016, driven largely by additional developed technology amortization associated with the acquisitions of Mozy in March 2018 and DoubleTake in January 2017, respectively.

Operating expenses

Research and development

| | Years Ended December 31, | | | 2018 Versus 2017 | | 2017 Versus 2016 | |
|---|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | Amount | % | Amount | % |
| | (in thousands, except percentage data) | | | | | | |
| Research and development | $ 57,467 | $ 46,160 | $ 33,298 | $ 11,307 | 24.5 % | $ 12,862 | 38.6 % |
| Percent of revenue | 19.4 % | 19.3 % | 16.1 % | | | | |
| Components of research and development: | | | | | | | |
| Personnel-related costs | $ 41,197 | $ 34,207 | $ 25,418 | $ 6,990 | 20.4 % | $ 8,789 | 34.6 % |
| Outside services and consulting costs | 8,514 | 3,876 | 2,443 | 4,638 | 119.7 % | 1,433 | 58.7 % |
| Hosting and other | 7,756 | 8,077 | 5,437 | (321 ) | (4.0 )% | 2,640 | 48.6 % |
| Total research and development | $ 57,467 | $ 46,160 | $ 33,298 | $ 11,307 | 24.5 % | $ 12,862 | 38.6 % |

Research and development expenses increased for the year ended December 31, 2018 as compared to the year ended December 31, 2017, driven largely by an increase in personnel-related costs associated with additional research and development headcount and an increase in outside services and consulting costs associated with the maintenance and integration of our solutions.

Research and development expenses increased for the year ended December 31, 2017, as compared to the year ended December 31, 2016, primarily due to an increase of personnel-related costs of $7.7 million associated with additional research and development headcount driven by the inclusion of acquired DoubleTake and Datacastle research and development employees and an increase of $1.1 million in stock-based compensation expense associated with new grants. Further, there was an increase in outside services and consulting costs associated with enhancing the functionality and ease of use of our solutions. Hosting and other costs increased $2.6 million driven largely by $0.8 million of acquisition and integration-related expenses associated with the acquisition of DoubleTake.

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General and administrative

| | Years Ended December 31, | | | 2018 Versus 2017 | | 2017 Versus 2016 | |
|---|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | Amount | % | Amount | % |
| | (in thousands, except percentage data) | | | | | | |
| General and administrative | $ 50,547 | $ 42,862 | $ 41,070 | $ 7,685 | 17.9 % | $ 1,792 | 4.4 % |
| Percent of revenue | 17.1 % | 17.9 % | 19.8 % | | | | |
| Components of general and administrative: | | | | | | | |
| Personnel-related costs | $ 28,077 | $ 24,515 | $ 21,471 | $ 3,562 | 14.5 % | $ 3,044 | 14.2 % |
| Professional fees | 12,408 | 11,503 | 11,255 | 905 | 7.9 % | 248 | 2.2 % |
| Consulting, taxes and other | 10,062 | 6,844 | 8,344 | 3,218 | 47.0 % | (1,500 ) | (18.0 )% |
| Total general and administrative | $ 50,547 | $ 42,862 | $ 41,070 | $ 7,685 | 17.9 % | $ 1,792 | 4.4 % |

General and administrative expenses increased for the year ended December 31, 2018 as compared to the year ended December 31, 2017, driven largely by a $1.9 million increase in stock-based compensation expense primarily associated with the achievement of performance goals and new grants and a $1.7 million increase in salaries and benefits included within personnel-related costs. The increase in these costs is driven by investment required to support our growth and operations as a public company. Further, there was a $1.1 million increase in hardware and software costs driven by recent acquisitions, a $0.7 million loss recorded on the sale of business, a $0.6 million increase in bad debt expense, and a $0.6 million increase in transactional tax expense owed to foreign tax authorities included within consulting, taxes and other.

General and administrative expenses increased for the year ended December 31, 2017, as compared to the year ended December 31, 2016, primarily as a result of increased personnel-related costs associated with additional headcount to support our overall growth and an increase of $1.7 million in stock-based compensation expense associated with new grants. The decrease in consulting, taxes and other expenses was driven by a decrease of $1.7 million in one-time transactional tax expense owed to foreign tax authorities, offset by an increase in hosting costs of $0.2 million.

Sales and marketing

| | Years Ended December 31, | | | 2018 Versus 2017 | | 2017 Versus 2016 | |
|---|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | Amount | % | Amount | % |
| | (in thousands, except percentage data) | | | | | | |
| Sales and marketing | $ 85,637 | $ 89,298 | $ 72,371 | $ (3,661 ) | (4.1 )% | $ 16,927 | 23.4 % |
| Percent of revenue | 28.9 % | 37.3 % | 35.0 % | | | | |
| Components of sales and marketing: | | | | | | | |
| Personnel-related costs | $ 39,006 | $ 42,350 | $ 31,828 | $ (3,344 ) | (7.9 )% | $ 10,522 | 33.1 % |
| Advertising costs | 16,959 | 16,416 | 17,833 | 543 | 3.3 % | (1,417 ) | (7.9 )% |
| Costs of credit card transactions and offering free trials | 8,786 | 7,275 | 6,508 | 1,511 | 20.8 % | 767 | 11.8 % |
| Marketing programs, consulting and other | 20,886 | 23,257 | 16,202 | (2,371 ) | (10.2 )% | 7,055 | 43.5 % |
| Total sales and marketing | $ 85,637 | $ 89,298 | $ 72,371 | $ (3,661 ) | (4.1 )% | $ 16,927 | 23.4 % |

Sales and marketing expenses decreased for the year ended December 31, 2018 as compared to the year ended December 31, 2017, driven largely by a decrease of $3.8 million in personnel-related costs and $0.7 million in marketing programs related to the adoption of Topic 606, as we now capitalize certain costs to obtain contracts with customers and amortize the costs over the period of benefit. There was a further decrease of $1.2 million in marketing program expenses as we focus on promoting our expanded set of business offerings through more efficient programs. These decreases were offset by increased credit card processing fees of $1.5 million associated with the acquisition of Mozy.

Sales and marketing expenses increased for the year ended December 31, 2017, as compared to the year ended December 31, 2016, primarily due to an increase in personnel-related costs associated with additional sales and marketing headcount driven by the inclusion of acquired DoubleTake sales and marketing employees. Additionally,

marketing programs, consulting and other costs increased by $7.1 million associated with promoting our expanded set of offerings and the inclusion of the DoubleTake business in our consolidated results. This increase was driven by an increase in consulting and independent contractor expenses of $1.8 million, travel and entertainment expenses of $1.3 million, software and hosted solutions expenses



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of $1.1 million, and integration and acquisition expenses of $1.0 million. Advertising costs declined related to a reduction in our traditional radio media spend compared to the year ended December 31, 2016.

Amortization of intangible assets

| | Years Ended December 31, | | | 2018 Versus 2017 | | 2017 Versus 2016 | |
|---|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | Amount | % | Amount | % |
| | (in thousands, except percentage data) | | | | | | |
| Amortization of intangible assets | $ 12,437 | $ 2,093 | $ 1,238 | $ 10,344 | 494.2 % | $ 855 | 69.1 % |
| As a % of total revenue | 4.2 % | 0.9 % | 0.6 % | | | | |

Amortization of intangible assets increased for the year ended December 31, 2018 as compared to the year ended December 31, 2017, and the year ended December 31, 2017 as compared to the year ended December 31, 2016, driven largely by an increase in amortization expense related to customer relationship and trade name assets associated with the acquisitions of Mozy in March 2018 and DoubleTake in January 2017, respectively.

Restructuring charges

| | Years Ended December 31, | | | 2018 Versus 2017 | | 2017 Versus 2016 | |
|---|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | Amount | % | Amount | % |
| | (in thousands, except percentage data) | | | | | | |
| Restructuring | $ 1,270 | $ 1,047 | $ 856 | $ 223 | 21.3 % | $ 191 | 22.3 % |
| As a % of total revenue | 0.4 % | 0.3 % | 0.4 % | | | | |

Restructuring expenses remained consistent for both the year ended December 31, 2018 as compared to the year ended December 31, 2017, and the year ended December 31, 2017, as compared to the year ended December 31, 2016.

Income (loss) from operations

Operating income for the year ended December 31, 2018 was $3.7 million, compared to an operating loss of $(12.1) million for the year ended December 31, 2017. The increase in operating income is primarily a result of an increase in revenue and a decrease in sales and marketing expenses.

Operating loss for the year ended December 31, 2017 was $(12.1) million compared to $(2.8) million for the year ended December 31, 2016. The increase in operating loss during the year ended December 31, 2017 is primarily a result of increases in sales and marketing expenses, research and development expenses, and costs of revenue.

Non-operating income (expense)

| | Years Ended December 31, | | | 2018 Versus 2017 | | 2017 Versus 2016 | |
|---|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | Amount | % | Amount | % |
| | (in thousands, except percentage data) | | | | | | |
| Interest expense | $ (11,556 ) | $ (7,447 ) | $ (147 ) | $ (4,109 ) | 55.2 % | $ (7,300 ) | 4,966.0 % |
| As a % of total revenue | (3.9 )% | (3.1 )% | (0.1 )% | | | | |
| Interest income | $ 1,877 | $ 581 | $ 25 | $ 1,296 | 223.1 % | $ 556 | 2,224.0 % |
| As a % of total revenue | 0.6 % | 0.2 % | — % | | | | |
| Other income (expense), net | $ 227 | $ 1,252 | $ 190 | $ (1,025 ) | (81.9 )% | $ 1,062 | 558.9 % |
| As a % of total revenue | 0.1 % | 0.5 % | 0.1 % | | | | |

Interest expense increased for the year ended December 31, 2018 as compared to the year ended December 31, 2017, primarily due to an increase in interest expense of $2.9 million related to our Convertible Notes issued in April 2017 and $1.2 million of interest expense related to our Revolving Credit Facility entered into in March 2018.

Interest expense increased for the year ended December 31, 2017, as compared to the year ended December 31, 2016, primarily due to interest expense of $7.2 million related to our Convertible Notes issued in April 2017.

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Interest income increased for the years ended December 31, 2018 and 2017 compared to the years ended December 31, 2017 and 2016, respectively, driven largely by interest income related to our highly liquid investments. Other income (expense), net primarily represents net foreign exchange gains and losses and other non-operating expense and income items. Other income (expense), net decreased for the year ended December 31, 2018 as compared to the year ended December 31, 2017, and increased for the year ended December 31, 2017 as compared to the year ended December 31, 2016, primarily due to a gain on the sale of businesses of $0.8 million, which took place in 2017.

(Benefit) provision for income taxes

| | Years Ended December 31, | | | 2018 Versus 2017 | | 2017 Versus 2016 | |
|---|---|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | Amount | % | Amount | % |
| | (in thousands, except percentage data) | | | | | | |
| (Benefit) provision for income taxes | $(13,347) | $(13,677) | $1,383 | $330 | (2.4)% | $(15,060) | (1,088.9)% |
| As a % of total revenue | (4.6)% | (5.7)% | 0.7% | | | | |

For the year ended December 31, 2018, our tax benefit was primarily driven by the recognition of a discrete tax benefit of $16.2 million due to the release of the U.S. valuation allowance as a result of the Mozy acquisition. For the year ended December 31, 2017, our tax benefit was primarily driven by a tax benefit for a U.S. valuation allowance release and refundable Federal Alternative Minimum Tax (“AMT”), partially offset by foreign income taxes. For the year ended December 31, 2016, our tax provision was primarily driven by foreign income taxes, Federal AMT, and state income taxes.

Liquidity and Capital Resources

As of December 31, 2018, we had cash and cash equivalents of $198.1 million, $172.0 million of which was held in the United States and $26.1 million of which was held by our international subsidiaries outside of the United States. If the undistributed earnings of our foreign subsidiaries are needed for our operations in the United States, we would be required to accrue and pay non-U.S. withholding taxes upon repatriation in certain non-U.S. jurisdictions. Our current plans are not expected to require repatriation of cash and investments to fund our U.S. operations and, as a result, we intend to permanently reinvest our foreign earnings to fund our foreign subsidiaries. Determination of the unrecognized deferred tax liability on unremitted earnings is not practical due to uncertainty regarding the remittance structure, the mix of earnings and earnings for profit pools in the year of remittance, and overall complexity of the calculation.

Source of funds

We believe, based on our current operating plan, that our existing cash and cash equivalents and cash provided by operations, as well as access to a new term loan and revolving credit facility that we expect to enter into in connection with the acquisition of Webroot, discussed below, will be sufficient to meet our anticipated cash needs for the foreseeable future.

On April 4, 2017, we issued, in a private offering, $143.8 million aggregate principal amount of Convertible Notes. The Convertible Notes accrue interest at 2.50% per year, payable semiannually in arrears on April 1 and October 1 of each year. The Convertible Notes will mature on April 1, 2022, unless earlier repurchased, redeemed or converted. At December 31, 2018, the Convertible Notes are not convertible.

In connection with the acquisition of Mozy, Inc., on March 19, 2018, we entered into a Revolving Credit Facility, which provides revolving credit financing of up to $130.0 million, including a $10.0 million sub-limit for letters of credit. The commitments under the Revolving Credit Facility may be increased by up to an additional $100.0 million plus an additional unlimited amount so long as the Company does not exceed a specified pro forma secured net leverage ratio, in either case provided the existing or additional lenders are willing to make such increased commitments and subject to other terms and conditions. The Revolving Credit Facility matures on the earlier of March 20, 2023 or 91 days prior to the maturity of the Company’s outstanding Convertible Notes. As of December 31, 2018, we had no outstanding borrowings under the Revolving Credit Facility. We intend to terminate the Revolving Credit Facility upon the execution of the Revolving Facility discussed below.

On February 7, 2019, we entered into an agreement and plan of merger to acquire Webroot for $618.5 million in cash to be adjusted with respect to cash, debt, transaction expenses and working capital. Concurrently with the execution of

the merger agreement, we entered into a financing commitment letter (the “Commitment Letter”) for (i) a seven-year senior secured term loan facility of $550.0 million (the “Term Loan Facility”) and (ii) a five-year senior secured revolving credit facility (the “Revolving Facility” and, together with the Term Loan Facility, the “Facilities”). Upon execution of the Revolving Facility, we intend to terminate our previously executed Revolving Credit Facility entered into on March 19, 2018. We will fund the

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transaction with existing cash and the Term Loan Facility. The Facilities will be subject to certain customary representations, warranties and covenants. The funding of the Facilities is subject to our compliance with customary terms and conditions precedent as set forth in the Commitment Letter, including the execution and delivery of definitive documentation consistent with the Commitment Letter and the substantially simultaneous consummation of the merger on terms consistent with the merger agreement.

On July 23, 2018, we issued and sold 4,765,157 shares of common stock in a public offering. An additional 819,485 shares were issued and sold pursuant to the underwriters' 30-day option on August 16, 2018. Proceeds of $199.3 million were recognized, net of underwriting discounts, commissions and offering expenses paid.

From time to time, we may explore additional financing sources to develop or enhance our solutions, fund expansion, respond to competitive pressures, acquire or to invest in complementary products, businesses or technologies, or to lower our cost of capital, which could include equity, equity-linked, and debt financing. There can be no assurance that any additional financing will be available to us on acceptable terms, if at all. If we raise additional funds through the issuance of equity or convertible debt or other equity-linked securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock.

Uses of funds

We have increased our operating and capital expenditures in connection with the growth in our operations and the increase in our personnel, and we anticipate that we will continue to increase such expenditures in the future. Our future capital requirements may vary materially from those now planned and will depend on many factors, including:

- potential future acquisition opportunities;
- potential share repurchases under our share repurchase plan;
- the levels of advertising and promotion required to acquire and retain customers;
- expansion of our data center infrastructure necessary to support our growth;
- growth of our operations in the U.S. and worldwide;
- our development and introduction of new solutions; and
- the expansion of our sales, customer support, research and development, and marketing organizations.

Future capital expenditures will focus on acquiring additional data storage and hosting capacity and general corporate infrastructure. We are not currently party to any purchase contracts related to future capital expenditures, other than short-term purchase orders.

Cash flows

The following table provides a summary and description of our net cash inflows (outflows) for 2018, 2017 , and 2016.

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | (in thousands) | | |
| Net cash provided by operating activities | 53,590 | 31,195 | 13,165 |
| Net cash (used in) investing activities | (160,030) | (91,655 ) | (16,275) |
| Net cash provided by (used in) financing activities | 176,830 | 127,622 | (1,404 ) |

Operating activities

Our cash flows from operating activities are significantly influenced by the amount of our net loss, growth in sales and customer growth, changes in working capital accounts, the timing of prepayments and payments to vendors, add-backs of non-cash expense items such as depreciation and amortization, and stock-based compensation expense.

In the year ended December 31, 2018 cash provided by operating activities was $53.6 million, which was driven by an increase in deferred revenue of $11.3 million, net income of $7.6 million and adjustments for non-cash charges of $51.6 million, primarily comprised of $41.8 million of depreciation and amortization, $17.6 million of stock-based compensation,

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$6.3 million of interest expense related to the non-cash interest expense related to the amortization of debt discount, $2.2 million of amortization of deferred costs, $0.6 million of impairment charges, partially offset by benefit for deferred income taxes of $16.6 million and a gain on disposal of equipment of $0.2 million, and other non-cash items of $0.1 million. These cash inflows were partially offset by a change in working capital items totaling $11.4 million, and a decrease in other assets and liabilities of $5.5 million.

In the year ended December 31, 2017, cash provided by operating activities was $31.2 million, which was driven by an increase in deferred revenue of $6.2 million, change in working capital items totaling $6.1 million and a net adjustment for non-cash charges of $23.5 million, primarily comprised of $21.7 million of depreciation and amortization, $12.7 million of stock-based compensation expense, $4.4 million of interest expense related to the non-cash interest expense related to the amortization of debt discount, $1.4 million of impairment charges, partially offset by a gain on disposal of equipment of $0.9 million, benefit for deferred income taxes of $15.4 million and other non-cash items of $0.5 million. These cash inflows were partially offset by our net loss of $4.0 million and a decrease in other assets and liabilities of $0.5 million.

In the year ended December 31, 2016, cash provided by operating activities was $13.2 million, which was driven by an increase in adjustments for non-cash charges of $25.6 million, primarily comprised of $15.9 million of depreciation and amortization, $8.9 million of stock-based compensation expense and other add-backs of $0.8 million, and an increase in deferred revenue of $2.4 million. The cash inflows were partially offset by our net loss of $4.1 million, a $0.6 million decrease in other assets and liabilities, and by changes in working capital items totaling $10.1 million, due to the timing of payments and customer receipts.

Investing activities

In the year ended December 31, 2018, cash used in investing activities was $160.0 million, which was primarily driven by our payment of $144.6 million in connection with the acquisition of Mozy, capital expenditures of $13.1 million, payments for intangible assets of $5.8 million, and purchases of derivatives of $1.4 million, partially offset by proceeds from maturities of derivatives of $4.0 million, and proceeds from the sale of property and equipment of $0.9 million.

In the year ended December 31, 2017, cash used in investing activities was $91.7 million, which was primarily driven by our payment of $69.8 million in connection with the acquisitions of DoubleTake and Datacastle, capital expenditures of $17.4 million, a purchases of derivatives of $5.0 million and a payment for intangible assets of $1.3 million, partially offset by proceeds from maturities of derivatives of $0.5 million, proceeds from sale of property and equipment and businesses of $1.3 million.

In the year ended December 31, 2016, cash used by investing activities was $16.3 million, consisting primarily of $11.6 million in cash that was paid for the EVault acquisition and $6.6 million for purchases of property and equipment. These uses of cash were partially offset by net proceeds from the purchase and sale of marketable securities and derivatives of $1.9 million.

Financing activities

In the year ended December 31, 2018 cash provided by financing activities was $176.8 million, which was primarily driven by $199.3 million in proceeds from the issuance of common shares related to our secondary offering, $88.1 million in proceeds from long-term borrowing, net of debt issuance costs, $2.6 million in proceeds from the issuance of treasury stock under our employee stock purchase plan, $1.3 million in proceeds from the exercise of stock options, partially offset by $90.0 million in payments on long-term borrowings, $21.5 million in repurchases of common stock and $2.9 million in payments of withholding taxes in connection with restricted stock unit vesting.

In the year ended December 31, 2017, cash provided by financing activities was $127.6 million, which was primarily driven by $177.8 million in proceeds from long-term borrowings, net of debt issuance costs, $5.0 million proceeds from the exercise of stock options and $1.0 million proceeds from issuance of treasury stock under our employee stock purchase plan, partially offset by $39.2 million payments on long-term borrowings, $15.0 million of repurchases of common stock and $2.0 million payments of withholding taxes in connection with restricted stock vesting.

In the year ended December 31, 2016 cash used in financing activities was $1.4 million, consisting of $4.5 million in cash used to repurchase common stock, $0.5 million payments of withholding taxes in connection with restricted stock vesting, offset by $3.6 million in proceeds received from the exercise of stock options.

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Contractual obligations

The following table summarizes our contractual obligations at December 31, 2018 (in thousands):

| | Payment Due by Period (1) | | | | |
|---|---|---|---|---|---|
| | Total | Less Than 1 Year | 1-3 Years | 3-5 Years | More Than 5 Years |
| | (in thousands) | | | | |
| Convertible notes principal | $143,750 | $— | $— | $143,750 | $— |
| Convertible notes interest | 12,579 | 3,594 | 7,188 | 1,797 | — |
| Office lease obligations | 24,608 | 4,194 | 7,863 | 7,368 | 5,183 |
| Data center lease obligations (2) | 12,303 | 4,833 | 6,567 | 903 | — |
| Hosted software obligations | 4,256 | 3,269 | 987 | — | — |
| Consulting obligations | 1,925 | 1,925 | — | — | — |
| Other purchase commitments | 13,082 | 12,875 | 207 | — | — |
| Total | $212,503 | $30,690 | $22,812 | $153,818 | $5,183 |

(1) See Note 12—Income Taxes to the consolidated financial statements included in this Annual Report for information related to our uncertain tax positions. The future payments related to uncertain tax positions have not been presented in the table above due to the uncertainty of the amounts and timing of cash settlement with the taxing authorities.

(2) Certain amounts in the table above relating to colocation leases for the Company's servers include usage based charges in addition to base rent.

The commitments under our office lease obligations shown above consist primarily of lease payments for our Boston, Massachusetts corporate headquarters, and our offices in Salt Lake City, Utah, Indianapolis, Indiana, and Mississauga, Ontario.

Commitments under our data center lease obligations included above consist primarily of Ashburn, Virginia; Chandler, Arizona; and St. George, Utah data centers. We also have data center colocation agreements in place to rent colocation space.

Additionally, we have non-cancellable commitments to vendors primarily consisting of hosted software obligations, consulting obligations, and other purchase commitments, which consist of contractual commitments to various vendors primarily for advertising, marketing, and broadband services.

Off-balance sheet arrangements

As of December 31, 2018, we did not have any off-balance sheet arrangements.

Critical Accounting Policies

Our consolidated financial statements are prepared in accordance with GAAP. The preparation of our financial statements and related disclosures requires us to make estimates, assumptions, and judgments that affect the reported amount of assets, liabilities, revenue, costs and expenses, and related disclosures. We base our estimates and assumptions on historical experience and other factors that we believe to be reasonable under the circumstances, but all such estimates and assumptions are inherently uncertain and unpredictable. We evaluate our estimates and assumptions on an ongoing basis. Actual results may differ from those estimates and assumptions, and it is possible that other professionals, applying their own judgment to the same facts and circumstances, could develop and support alternative estimates and assumptions that would result in material changes to our operating results and financial condition.

The critical accounting policies requiring estimates, assumptions, and judgments that we believe have the most significant impact on our consolidated financial statements are described below. Refer to Note 2—Summary of Significant Accounting Policies to our consolidated financial statements included in this Annual Report for additional information related to our accounting policies and our consideration of these critical accounting areas.

Revenue Recognition

We generate substantially all of our revenues from contracts with customers. We derive our revenue from cloud-hosted subscription services, software licenses, customer support services and software enhancements (i.e. maintenance), implementation and training services, and sales of hardware. We recognize revenue when we transfer control of the promised

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goods or services to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for those products or services. We initially assess each contract to identify any and all goods or services within, and then evaluate whether those goods and services are distinct, or capable of being distinct within the context of the contract. A good or service that is promised to a customer is distinct if the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer, and a company's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract. Goods and services that are identified as being distinct are identified as contractual performance obligations. Goods and services that are not both capable of being distinct and distinct within the context of the contract are combined and treated as a single performance obligation in determining the allocation and recognition of revenue. We allocate the transaction price to each distinct performance obligation based on the standalone selling price ("SSP") of each good or service.

The SSP is the price at which we would sell a promised product or service separately to the customer. For the majority of our cloud-hosted subscription services and maintenance offerings, we use the observable price when we sell that support and service and cloud-hosted subscription separately to similar customers. If the SSP for a performance obligation is not directly observable, we estimate it. We estimate the SSP by taking into consideration market conditions, economics of the offering and customers' behavior. We maximize the use of observable inputs and apply estimation methods consistently in similar circumstances. We allocate the transaction price to each distinct performance obligation on a relative standalone selling price basis. Refer to Note 2—Summary of Significant Accounting Policies to our consolidated financial statements for further information on our revenue recognition.

Costs to Obtain a Contract with a Customer

Sales commissions earned by our sales teams are considered incremental, recoverable costs of obtaining a contract with a customer. Sales commissions for initial contracts are deferred and then amortized on a straight-line basis over a period of benefit that we have determined to be approximately six years. The six year period has been determined by taking into consideration the type of product sold, the commitment term of the customer contract, the nature of our technology development life-cycle, and an estimated customer relationship period. Sales commissions for upgrade and renewal contracts are expensed in the period incurred. While we do not anticipate any significant changes to the six year amortization period, if a change did occur it could produce a material impact on our financial statements.

Business Combinations

In accordance with ASC 805, Business Combinations ("ASC 805"), we recognize identifiable assets acquired and liabilities assumed at their acquisition date fair value. Fair value determinations involve significant estimates and assumptions about several highly subjective variables, including future cash flows, discount rates, and expected business performance. There are also different valuation models and inputs for each component, the selection of which requires considerable judgment. These determinations will affect the amount of amortization expense recognized in future periods. While we use our best estimates and assumptions as part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the acquisition date, our estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, we record adjustments to the assets acquired and liabilities assumed with the corresponding offset to goodwill to the extent that we identify adjustments to the preliminary purchase price allocation. Upon the conclusion of the measurement period or final determination of the values of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the consolidated statements of operations.

Goodwill and acquired intangible assets

We record goodwill when consideration paid in a business acquisition exceeds the value of the net assets acquired. Our estimates of fair value are based upon assumptions believed to be reasonable at that time, but that are inherently uncertain and unpredictable. Assumptions may be incomplete or inaccurate, and unanticipated events or circumstances may occur, which may affect the accuracy or validity of such assumptions, estimates or actual results.

Goodwill is not amortized, but rather is tested for impairment annually or more frequently at the reporting unit level if facts and circumstances warrant a review. We have determined that there is a single reporting unit for the purpose of conducting this goodwill impairment assessment. We estimate the fair value of the reporting unit (based on our market capitalization) and compare this amount to the carrying value of the reporting unit (as reflected by our total

stockholders' equity). If we determine that the carrying value of the reporting unit exceeds its fair value, an impairment charge would be required. Our annual goodwill impairment test is performed at November 30 of each year. To date, we have not identified any impairment to goodwill.

Intangible assets acquired in a business combination are recorded at their estimated fair values at the date of acquisition. We amortize acquired intangible assets over their estimated useful lives based on the pattern of consumption of the economic

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benefits or, if that pattern cannot be readily determined, on a straight-line basis. We review our intangible assets with definite lives for impairment when events or changes in circumstances indicate that the related carrying amount of any of these assets may not be recoverable. The details of our intangible asset impairment assessment are included in Note 5 - Fair Value of Financial Instruments.

Income taxes

We provide for income taxes under the liability method. Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates in effect when the differences are expected to reverse. In certain jurisdictions, deferred tax assets are reduced by a valuation allowance to reflect the uncertainty associated with their ultimate realization. We account for uncertain tax positions recognized in our consolidated financial statements by prescribing a more-likely-than-not threshold for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. If actual results differ from estimates we have used, or if we adjust these estimates in future periods, our operating results and financial position could be materially affected.

Due to a history of losses, we have provided a full valuation allowance against our deferred tax assets in the U.S. and in certain foreign jurisdictions that are in a deferred tax asset position for which we are uncertain as to their ultimate realization. This is more fully described in Note 12 - Income Taxes to our consolidated financial statements, included in the Annual Report. The ability to utilize these deferred tax assets may be restricted or eliminated by changes in our ownership, changes in legislation, and other rules affecting the ability to offset future taxable income with losses or other tax attributes from prior periods. Future determinations on the need for a valuation allowance on our net deferred tax assets will be made on an annual basis.

Stock-based compensation

We recognize stock-based compensation as an expense in the financial statements using the estimated grant-date fair value over the individual award's requisite service period, which equals the vesting periods in all cases but for certain market-based awards. We use the straight-line amortization method for recognizing stock-based compensation expense. We estimate the fair value of stock options on the date of grant using the Black-Scholes option-pricing model and the fair value of stock options and awards with market-based vesting conditions on the date of grant using a Monte Carlo simulation. These models require the use of highly subjective estimates and assumptions, including expected stock price volatility, expected term of an award, risk-free interest rate, and expected dividend yield. The grant date fair value of restricted stock units granted is based on the fair value of the underlying common stock on the date of grant.

Recent Accounting Pronouncements

For information on recent accounting pronouncements, refer to Note 2 - Summary of Significant Accounting Policies - Recently Issued Accounting Pronouncements in the notes to the consolidated financial statements included in this Annual Report.

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ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risks in the ordinary course of our business. The most significant market risk we face is foreign currency exchange risk and to a lesser degree, interest rate fluctuation risk.

Foreign Currency Exchange Risk

We are exposed to foreign currency exchange rate risk inherent in our revenues, expenses, sales commitments, anticipated sales, anticipated purchases, and assets and liabilities denominated in currencies other than the U.S. dollar, primarily the Euro. In addition, we are exposed to foreign currency exchange rate risk, in connection with assets and liabilities of our wholly owned subsidiaries, that are denominated in currencies other than the local and/or functional currency of the entity. These transactions and balances are subject to foreign currency exchange gains and losses when remeasured into local currencies and/or translated into U.S. dollars. Assets and liabilities of our foreign entities are translated into U.S. dollars at exchange rates in effect at the balance sheet date, and income and expense items are translated at average rates for the applicable period. Fluctuations in foreign currency exchange rates may cause us to recognize transaction and/or translation gains and losses in our statements of operations, as well as our statements of other comprehensive loss.

We routinely enter into short-term foreign currency forward contracts to offset foreign exchange gains and losses generated by the remeasurement of certain intercompany loans denominated in non-functional currencies. These contracts are not designated as cash flow or fair value hedges and have historically been for periods of less than one year. Changes in the fair value of these derivatives, as well as remeasurement gains and losses on the underlying intercompany assets and liabilities, are recognized in our consolidated statements of operations within "other income (expense), net". At December 31, 2018 and 2017, we had outstanding contracts with a total notional value of $43.8 million and $47.8 million, respectively.

We have performed a sensitivity analysis as of December 31, 2018, using a modeling technique that measures hypothetical gains and losses for a one-year period, from a 10% movement in foreign currency exchange rates relative to the U.S. dollar and applicable functional currencies of our subsidiaries that hold assets and/or liabilities in non-functional currencies. The foreign currency exchange rates we used were based on market rates in effect on December 31, 2018. We estimate that a hypothetical 10% adverse change in foreign currency exchange rates, based upon our market risk as it existed as of December 31, 2018 would result in an immaterial adverse impact on income (loss) from operations in our consolidated statements of operations.

While we have implemented strategies to mitigate certain risks associated with fluctuations in foreign currency exchange rates, we cannot ensure that we will not recognize gains or losses from international transactions, as this risk is part of transacting business in an international environment. Our policy does not allow speculation in derivative instruments for profit or execution of derivative instrument contracts for which there are no underlying exposures. We do not use financial instruments for trading purposes and are not party to any leveraged derivatives. Not every exposure is or can be hedged and, where hedges are put in place based on expected foreign exchange exposure, they are based on forecasts for which actual results may differ from the original estimate. Failure to successfully hedge or anticipate currency risks properly could affect our consolidated operating results.

As we increase our operations in international markets, our exposure to potentially volatile movements in foreign currency exchange rates increases. The economic impact to us of foreign currency exchange rate movements is linked to variability in real growth, inflation, interest rates, governmental actions and other factors. These changes, if significant, could cause us to adjust our foreign currency risk strategies.

Interest Rate Risk

We are exposed to interest rate risk as a result of our cash and cash equivalents. Our cash equivalents consist of cash and money market funds. The money market funds are invested solely in U.S. agency and treasury securities. As of December 31, 2018, the carrying amount of our cash equivalents reasonably approximates fair value and have a constant $1 net asset value ("NAV") with daily liquidity. The primary objective of our investment policy is to preserve principal, while maximizing income and minimizing risk. Accordingly, due to the nature of our cash equivalents, they are relatively insensitive to interest rate changes. We have conducted a rate sensitivity analysis of our interest rate fluctuation, and have determined that the risk of a 10% increase or decrease in interest rates would not have a material effect on the fair market value of our portfolio.

Our Convertible Notes have a fixed annual interest rate of 2.5%, and, therefore, we do not have interest rate exposure on the Convertible Notes. On March 19, 2018, we entered into a Revolving Credit Facility which provides revolving credit financing of up to $130.0 million, including a $10.0 million sub-limit for letters of credit and a $10.0 million sub-limit for swingline loans. As of December 31, 2018, we had no outstanding borrowings under the Revolving Credit Facility and therefore no interest rate exposure.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA
Carbonite, Inc.
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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the stockholders and the Board of Directors of Carbonite, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Carbonite, Inc. and subsidiaries (the "Company") as of December 31, 2018 and 2017, the related consolidated statements of operations, comprehensive income (loss), stockholders' equity, and cash flows for the years ended December 31, 2018 and 2017 and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the two years ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 28, 2019, expressed an unqualified opinion on the Company's internal control over financial reporting.

Change in Accounting Principles

As discussed in Note 2 to the consolidated financial statements, the Company has changed its method of accounting for revenue from contracts with customers and costs to obtain a contract, using the modified retrospective approach, upon the adoption of Accounting Standards Update 2014-09, Revenue from Contracts with Customers as of January 1, 2018.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Deloitte & Touche LLP

Boston, Massachusetts
February 28, 2019
We have served as the Company's auditor since 2017.



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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders of
Carbonite, Inc.

We have audited the accompanying consolidated statements of operations, comprehensive loss, stockholders' equity and cash flows for the year ended December 31, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated results of Carbonite, Inc.'s operations and its cash flows for the year ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young LLP

Boston, Massachusetts
March 16, 2017,
except for the effects of the adoption of ASU 2016-09 as discussed in Note 2, as to which the date is March 12, 2018 and for the effects of the adoption of ASU 2016-18 as discussed in Note 2 and for the effects of the revision of prior period amounts as discussed in Note 3, as to which the date is February 28, 2019

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Carbonite, Inc.
Consolidated Balance Sheets

| | December 31, | |
|---|---|---|
| | 2018 | 2017 |
| | (In thousands, except share and per share data) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 198,087 | $ 128,231 |
| Trade accounts receivable, less allowances of $892 and $994 | 31,569 | 22,219 |
| Prepaid expenses and other current assets | 10,409 | 6,823 |
| Total current assets | 240,065 | 157,273 |
| Property and equipment, net | 34,101 | 28,790 |
| Other assets | 13,876 | 804 |
| Acquired intangible assets, net | 117,963 | 44,994 |
| Goodwill | 155,086 | 80,958 |
| Total assets | $ 561,091 | $ 312,819 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | $ 2,114 | $ 10,842 |
| Accrued compensation | 11,620 | 9,892 |
| Accrued expenses and other current liabilities | 15,844 | 11,783 |
| Current portion of deferred revenue | 121,553 | 100,241 |
| Total current liabilities | 151,131 | 132,758 |
| Long-term debt | 118,305 | 111,819 |
| Deferred revenue, net of current portion | 29,151 | 24,273 |
| Other long-term liabilities | 5,294 | 5,704 |
| Total liabilities | 303,881 | 274,554 |
| Commitments and contingencies (Note 13) | | |
| Stockholders' equity: | | |
| Preferred stock, $0.01 par value; 6,000,000 shares authorized; no shares issued | — | — |
| Common stock, $0.01 par value; 45,000,000 shares authorized; 36,641,317 shares issued and 33,923,135 shares outstanding at December 31, 2018; 30,130,856 shares issued and 28,182,094 shares outstanding at December 31, 2017 | 366 | 301 |
| Additional paid-in capital | 451,618 | 233,343 |
| Treasury stock, at cost (2,718,182 and 1,948,762 shares as of December 31, 2018 and 2017, respectively) | (48,522) | (26,616) |
| Accumulated other comprehensive income | 1,650 | 581 |
| Accumulated deficit | (147,902) | (169,344) |
| Total stockholders' equity | 257,210 | 38,265 |
| Total liabilities and stockholders' equity | $ 561,091 | $ 312,819 |

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

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Carbonite, Inc.
Consolidated Statements of Operations

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | (In thousands, except share and per share data) | | |
| Revenue: | | | |
| Services | $263,084 | $207,403 | $186,087 |
| Product | 33,324 | 32,059 | 20,899 |
| Total revenue | 296,408 | 239,462 | 206,986 |
| Cost of revenue: | | | |
| Services | 68,024 | 59,212 | 55,512 |
| Product | 1,730 | 2,676 | 2,793 |
| Amortization of intangible assets | 15,629 | 8,179 | 2,632 |
| Total cost of revenue | 85,383 | 70,067 | 60,937 |
| Gross profit | 211,025 | 169,395 | 146,049 |
| Operating expenses: | | | |
| Research and development | 57,467 | 46,160 | 33,298 |
| General and administrative | 50,547 | 42,862 | 41,070 |
| Sales and marketing | 85,637 | 89,298 | 72,371 |
| Amortization of intangible assets | 12,437 | 2,093 | 1,238 |
| Restructuring charges | 1,270 | 1,047 | 856 |
| Total operating expenses | 207,358 | 181,460 | 148,833 |
| Income (loss) from operations | 3,667 | (12,065) | (2,784) |
| Interest expense | (11,556) | (7,447) | (147) |
| Interest income | 1,877 | 581 | 25 |
| Other income (expense), net | 227 | 1,252 | 190 |
| Loss before income taxes | (5,785) | (17,679) | (2,716) |
| (Benefit) provision for income taxes | (13,347) | (13,677) | 1,383 |
| Net income (loss) | $7,562 | $(4,002) | $(4,099) |
| Basic net income (loss) per share attributable to common stockholders | $0.24 | $(0.14) | $(0.15) |
| Diluted net income (loss) per share attributable to common stockholders | $0.22 | $(0.14) | $(0.15) |
| Weighted-average number of common shares used in computing basic net income (loss) per share | 31,036,237 | 27,779,098 | 27,028,636 |
| Weighted-average number of common shares used in computing diluted net income (loss) per share | 33,672,686 | 27,779,098 | 27,028,636 |

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

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Carbonite, Inc.
Consolidated Statements of Comprehensive Income (Loss)

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | (In thousands) | | |
| Net income (loss) | $7,562 | $(4,002) | $(4,099) |
| Other comprehensive income (loss): | | | |
| Foreign currency translation adjustments | 1,069 | (2,736) | 1,277 |
| Total other comprehensive income (loss) | 1,069 | (2,736) | 1,277 |
| Total comprehensive income (loss) | $8,631 | $(6,738) | $(2,822) |

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

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Carbonite, Inc.
Consolidated Statements of Stockholders' Equity

| | Common Stock | | Additional Paid-in Capital | Accumulated Deficit | Treasury Stock | Accumulated Other Comprehensive Income | Total Stockholders' Equity |
|---|---|---|---|---|---|---|---|
| | Number of Shares | Amount | | | | | |
| in thousands, except share data | | | | | | | |
| Balance at December 31, 2015 | 27,756,799 | $ 278 | $ 165,391 | $ (160,943 ) | $ (5,693 ) | $ 2,040 | $ 1,073 |
| Stock options exercised and vesting of restricted stock units | 788,290 | 7 | 3,553 | | | | 3,560 |
| Stock-based compensation expense | | | 8,983 | | | | 8,983 |
| Tax benefits relating to share-based payments | | | 4 | | | | 4 |
| Acquisition of treasury stock | | | | | (4,481 ) | | (4,481 ) |
| Payments of withholding taxes in connection with restricted stock unit vesting | | | | | (483 ) | | (483 ) |
| Other comprehensive income | | | | | | 1,277 | 1,277 |
| Net loss | | | | (4,099 ) | | | (4,099 ) |
| Balance at December 31, 2016 | 28,545,089 | 285 | 177,931 | (165,042 ) | (10,657 ) | 3,317 | 5,834 |
| Stock options exercised and vesting of restricted stock units | 1,253,441 | 13 | 4,974 | | | | 4,987 |
| Issuance of common stock related to business combinations | 332,326 | 3 | 5,730 | | | | 5,733 |
| Stock-based compensation expense | | | 12,841 | | 119 | | 12,960 |
| Issuance of treasury stock in connection with employee stock purchase plan | | | 116 | | 936 | | 1,052 |
| Acquisition of treasury stock | | | | | (14,964 ) | | (14,964 ) |
| Payments of withholding taxes in connection with restricted stock unit vesting | | | | | (2,050 ) | | (2,050 ) |
| Allocation of equity component related to Convertible Notes | | | 31,451 | | | | 31,451 |
| Adjustment resulting from the adoption of ASU 2016-09 | | | 300 | (300 ) | | | — |
| Other comprehensive loss | | | | | | (2,736 ) | (2,736 ) |
| Net loss | | | | (4,002 ) | | | (4,002 ) |
| Balance at December 31, 2017 | 30,130,856 | 301 | 233,343 | (169,344 ) | (26,616 ) | 581 | 38,265 |
| Stock options exercised and vesting of restricted stock units | 925,819 | 9 | 1,251 | | | | 1,260 |
| Issuance of common stock associated with secondary offering | 5,584,642 | 56 | 199,223 | | | | 199,279 |
| Stock-based compensation expense | | | 17,518 | | 154 | | 17,672 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Issuance of treasury stock in connection with employee stock purchase plan | | | 283 | | 2,303 | | 2,586 |
| Acquisition of treasury stock | | | | | (21,501 ) | | (21,501 ) |
| Payments of withholding taxes in connection with restricted stock unit vesting | | | | | (2,862 ) | | (2,862 ) |
| Adjustment resulting from the adoption of Topic 606 | | | | 13,880 | | | 13,880 |
| Other comprehensive income | | | | | | 1,069 | 1,069 |
| Net income | | | | 7,562 | | | 7,562 |
| Balance at December 31, 2018 | 36,641,317 | $ 366 | $ 451,618 | $ (147,902 ) | $ (48,522 ) | $ 1,650 | $ 257,210 |

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

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Carbonite, Inc.
Consolidated Statements of Cash Flows

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | (In thousands) | | |
| Operating activities | | | |
| Net income (loss) | $7,562 | $(4,002) | $(4,099) |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | | |
| Depreciation and amortization | 41,786 | 21,731 | 15,869 |
| Amortization of deferred costs | 2,166 | — | — |
| (Gain) loss on disposal of equipment | (191) | (907) | 748 |
| Intangible asset impairment charges | — | 352 | — |
| Impairment of capitalized software | 653 | 1,048 | — |
| Stock-based compensation expense | 17,607 | 12,742 | 8,900 |
| Benefit for deferred income taxes | (16,625) | (15,392) | (15) |
| Non-cash interest expense related to amortization of debt discount | 6,340 | 4,434 | — |
| Other non-cash items, net | (139) | (533) | 68 |
| Changes in assets and liabilities, net of acquisitions: | | | |
| Accounts receivable | (5,996) | 1,786 | (13,412) |
| Prepaid expenses and other current assets | (3,718) | 254 | (1,547) |
| Other assets | (5,241) | (580) | 17 |
| Accounts payable | (7,359) | 5,035 | (3,345) |
| Accrued expenses | 5,636 | (995) | 8,183 |
| Other long-term liabilities | (236) | 53 | (586) |
| Deferred revenue | 11,345 | 6,169 | 2,384 |
| Net cash provided by operating activities | 53,590 | 31,195 | 13,165 |
| Investing activities | | | |
| Purchases of property and equipment | (13,132) | (17,351) | (6,582) |
| Proceeds from sale of property and equipment and businesses | 860 | 1,250 | 13 |
| Proceeds from maturities of marketable securities and derivatives | 4,017 | 534 | 3,395 |
| Purchases of derivatives | (1,428) | (5,040) | (1,476) |
| Payment for intangibles | (5,750) | (1,250) | — |
| Payment for acquisitions, net of cash acquired | (144,597) | (69,798) | (11,625) |
| Net cash used in investing activities | (160,030) | (91,655) | (16,275) |
| Financing activities | | | |
| Proceeds from exercise of stock options | 1,260 | 4,987 | 3,560 |
| Proceeds from issuance of common shares for secondary offering | 199,279 | — | — |
| Proceeds from issuance of treasury stock under employee stock purchase plan | 2,586 | 1,052 | — |
| Payments of withholding taxes in connection with restricted stock unit vesting | (2,862) | (2,050) | (483) |
| Proceeds from long-term borrowing, net of debt issuance costs | 88,068 | 177,797 | — |
| Payments on long-term borrowings | (90,000) | (39,200) | — |
| Repurchase of common stock | (21,501) | (14,964) | (4,481) |
| Net cash provided by (used in) financing activities | 176,830 | 127,622 | (1,404) |
| Effect of currency exchange rate changes on cash | (534) | 1,782 | (270) |
| Net increase (decrease) in cash, cash equivalents and restricted cash | 69,856 | 68,944 | (4,784) |
| Cash, cash equivalents and restricted cash, beginning of period | 128,231 | 59,287 | 64,071 |

| | | | |
|---|---|---|---|
| Cash, cash equivalents and restricted cash, end of period | $198,087 | $128,231 | $59,287 |

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

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Carbonite, Inc.
Consolidated Statements of Cash Flows (continued)

| | | | |
|---|---|---|---|
| Supplemental disclosure of cash flow information | | | |
| Cash paid for income taxes | $542 | $820 | $1,160 |
| Cash paid for interest | $4,762 | $1,767 | $— |
| Supplemental disclosure of non-cash investing and financing activities | | | |
| Capitalization of stock-based compensation | $65 | $218 | $83 |
| Acquisition of property and equipment included in accounts payable and accrued expenses | $(146 ) | $(641 ) | $894 |
| Issuance of common stock for acquisition | $— | $5,733 | $— |

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

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Carbonite, Inc.
Notes to Consolidated Financial Statements
1. Nature of Business
The Company was incorporated in the State of Delaware on February 10, 2005 and provides robust backup, disaster recovery, high availability and workload migration solutions (the "Carbonite Data Protection Platform"). The Carbonite Data Protection Platform supports businesses on a global scale with secure cloud infrastructure.
The Company views its operations and manages its business as one operating segment.
2. Summary of Significant Accounting Policies
Principles of Consolidation
The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) and include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts and transactions between the Company and its subsidiaries have been eliminated in consolidation.
During 2016, the Company recorded an adjustment for payments owed to foreign tax authorities inclusive of any interest and penalties that were not accrued for in prior fiscal years. This adjustment was recorded as an increase to accrued liabilities for approximately $1.2 million with a corresponding expense recorded in general and administrative expenses in the condensed consolidated statements of operations. Of this $1.2 million adjustment, approximately $0.2 million related to the year ended December 31, 2015 and $1.0 million related to prior years. The Company concluded the effect of these adjustments were not material to its consolidated financial statements for the current period or any of the prior periods.
Use of Estimates
The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Although the Company regularly assesses these estimates, actual results could differ materially from these estimates. Changes in estimates are recorded in the period in which they become known. The Company bases its estimates on historical experience and various other assumptions that it believes to be reasonable under the circumstances. Actual results may differ from management’s estimates if past experience or other assumptions do not turn out to be substantially accurate, even if such assumptions are reasonable when made.
Translation of Foreign Currencies
The functional currency of the Company’s foreign subsidiaries is generally the local currency in which they operate. The Company translates foreign subsidiaries' assets and liabilities at the exchange rates in effect at period-end and revenues and expenses at the average exchange rates in effect during the period. Gains and losses from foreign currency translation are recorded as a component of other comprehensive income (loss).
Foreign currency transaction gains and losses are included in other income (expense), net in the consolidated statements of operations, net of losses and gains from any related derivative financial instruments. Transaction (losses) gains were $(2.7) million, $5.1 million and $(0.8) million during the years ended December 31, 2018, 2017, and 2016, respectively.
Concentration of Credit Risk
Financial instruments that potentially subject the Company to credit risk primarily consist of cash and cash equivalents, derivatives, and accounts receivable. The Company maintains its cash and cash equivalents and derivatives with high-quality financial institutions and, consequently, the Company believes that such funds are subject to minimal credit risk. Cash equivalents consist of investment grade debt securities or money market funds investing in such securities.
The Company regularly reviews its accounts receivable related to customers billed on traditional credit terms and provides an allowance for expected credit losses. Due to these factors, no additional credit risk beyond amounts provided for collection losses is believed by management to be probable in the Company’s accounts receivable. No customer represented 10% or more of the Company’s accounts receivable balance as of December 31, 2018 and 2017. Further, no customer represented 10% or more of the Company's revenue for the years ended December 31, 2018,

2017, and 2016.

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Revenue Recognition

The Company primarily sells products and services as discussed below. Each category contains one or more performance obligation that is either (i) capable of being distinct (i.e., the customer can benefit from the good or service on its own or together with readily available resources, including those purchased separately from the Company) and distinct within the context of the contract (i.e., separately identifiable from other promises in the contract), or (ii) a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. Aside from software licenses and hardware, which are delivered at a point in time, the majority of the Company's other services are delivered over time.

Under ASU 2014-09, Revenue from Contracts with Customers (Topic 606) ("Topic 606"), the Company recognizes revenue following a five step model, as outlined below:

- Identify the contract.
- Identify the performance obligations.
- Determine the transaction price.
- Allocate the transaction price.
- Recognize revenue.

Identifying the Contract

The Company considers itself to have a contract with a customer when all of the following are met:

- The parties have approved the contract;
- The Company can identify each party's rights regarding the goods or services to be transferred;
- The Company can identify the payment terms;
- The contract has commercial substance; and
- It is probable that the Company will collect substantially all of the consideration to which it will be entitled.

Performance Obligations and Timing of Revenue Recognition

Service Revenue

The Company offers SaaS and HaaS offerings. Most notably, the Company offers the customer the right to access its software through its SaaS offering, where the Company hosts the software and the customer is granted access via the web. Control of the software does not transfer in these types of arrangements and is therefore not considered a distinct performance obligation. Revenues related to the SaaS and HaaS offerings are recorded over the performance period of the services.

The Company also offers M&S services for its licenses. M&S services generally consist of telephone, email, or live chat support, as well as updates and upgrades to the software licenses on an if and when available basis. All M&S obligations are considered distinct performance obligations that are of substantially the same duration and measure of progress and are therefore combined into a single performance obligation. As such, revenues from M&S are recorded ratably over the time of performance.

The Company also offers professional services to customers consisting of implementation, training, migration and protection services, and consulting. Professional services are regularly sold in conjunction with other products or services, as well as on a standalone basis and either (i) prepaid upfront or (ii) sold on a time and materials basis. Professional service revenue is recognized over time as services are delivered. For time and materials-based consulting arrangements, the Company has elected the practical expedient of recognizing revenue upon invoicing since the invoiced amount corresponds directly to the value of the Company's service to date.

Product Revenue

The Company sells different types of on-premise data protection and migration software, licensed on a term or perpetual basis, and as royalty arrangements. License arrangements generally include maintenance and support services, but the software is fully functional upon delivery and is considered to be a distinct performance obligation. Revenues from product licenses are recorded when control of the product has been transferred to the customer.

The Company also offers hardware on a standalone basis or in conjunction with the Company's software. Hardware sales are recorded as revenue when control is transferred to the customer.

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Determining the Transaction Price

To determine the transaction price, the Company considers both fixed and variable consideration. The majority of the Company's contracts contain fixed consideration that is paid up-front. Variable consideration is included in the transaction price to the extent it is probable that a significant reversal will not occur. The Company has the following sources of variable consideration:

Performance penalties - Subscription services and product support arrangements generally contain performance response time guarantees. For subscription services arrangements, the Company estimates variable consideration using a portfolio approach because performance penalties are tied to standard response time requirements. For product support arrangements, the Company estimates variable consideration on a contract basis because such arrangements are customer-specific. For both subscription services and product support arrangements, the Company uses an expected value approach to estimate variable consideration based on historical business practices and current and future performance expectations to determine the likelihood of incurring penalties.

Extended payment terms - The Company's standard payment terms are generally within 90 days of invoicing. If extended payment terms are granted to customers, those terms generally do not exceed one year. For contracts with extended payment terms, the Company estimates variable consideration on a contract basis because such estimates are customer-specific, and uses an expected value approach to analyze historical business experience on a customer-by-customer basis to determine the likelihood that extended payment terms lead to an implied price concession.

Sales and usage-based royalties - Certain product license arrangements include sales or usage-based royalties, covering both the software license and product support. Typically, the arrangements consist of a minimum commitment as well as usage based "overage" fees. The Company includes the minimum commitments in determining the transaction price, however, excludes an estimate of sales or usage based "overages".

The Company has elected to exclude taxes assessed by government authorities in determining the transaction price, and therefore revenue is recognized net of taxes collected from customers.

Allocating the Transaction Price

The Company allocates the transaction price to each performance obligation based on the standard selling price ("SSP"), which is the price the Company regularly sells the product or service on a standalone basis. For certain products or services, a readily identifiable SSP is not available. In such cases, the Company estimates the SSP using the following methodologies:

Product licenses - Product licenses are not sold on a standalone basis. The Company establishes the SSP of product licenses using a residual approach after first establishing the SSP of the associated maintenance and support. Maintenance and support is sold on a standalone basis as annual renewals, and because an economic relationship exists between product licenses and maintenance and support, the Company has concluded that the residual method to estimate the SSP of product licenses sold on both a perpetual and term basis is an appropriate allocation of the transaction price.

Maintenance and Support (time-based licenses) - The Company establishes the SSP of maintenance and support included in time-based licenses based on similar percentages charged for maintenance and support of perpetual licenses because time-based licenses, when renewed, are renewed for the right to use the license as well as the ongoing maintenance and support. The Company believes this method is an appropriate allocation of maintenance and support in time-based license arrangements.

The Company infrequently provides options to purchase future products or services at a discount. The Company analyzes the option price against the SSP of the previously established goods or services to determine if the options represent material rights that should be accounted for as separate performance obligations. In general, options sold at or above the SSP are not considered separate performance obligations because the customer could have received that right without entering into the contract. If a material right exists, revenue associated with the option is recognized when the future goods or services are transferred, or when the option expires.

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with an original purchase maturity of 90 days to be the equivalent of cash for the purpose of balance sheet and statement of cash flows presentation.

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Property and Equipment

Property and equipment are stated at cost. Expenditures for repairs and maintenance are charged to expense as incurred. Upon retirement or sale, the cost of the assets disposed of and the related accumulated depreciation and amortization are eliminated from the accounts and any resulting gain or loss is reflected in the consolidated statement of operations.

Depreciation and amortization is calculated using the straight-line method over the estimated useful lives of the assets, which are as follows:

| Asset Classification | Estimated Useful Life |
| --- | --- |
| Computer equipment | 2 - 4 years |
| Appliances | 3 years |
| Purchased software | 3 years |
| Internal-use software | 2 - 7 years |
| Furniture and fixtures | 5 years |
| Leasehold improvements | Shorter of useful life or remaining life of lease |

Impairment of Long-Lived Assets

The Company reviews property and equipment and intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the recoverability of these assets is considered to be impaired, the impairment to be recognized equals the amount by which the carrying value of the assets exceeds their estimated fair value. The details of the Company's impairment assessment are included in Note 5 - Fair Value of Financial Instruments.

Business Combinations

In accordance with ASC 805, Business Combinations ("ASC 805"), the Company recognizes tangible and intangible assets acquired and liabilities assumed based on their estimated fair values. Determining these fair values requires management to make significant estimates and assumptions, especially with respect to intangible assets.

The Company recognizes identifiable assets acquired and liabilities assumed at their acquisition date fair value. Goodwill as of the acquisition date is measured as the excess of consideration transferred over the net of the acquisition date fair value of the assets acquired and the liabilities assumed and represents the expected future economic benefits arising from other assets acquired that are not individually identified and separately recognized. While the Company uses its best estimates and assumptions as part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the acquisition date, its estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, the Company records adjustments to the assets acquired and liabilities assumed with the corresponding offset to goodwill to the extent that it identifies adjustments to the preliminary purchase price allocation. Upon the conclusion of the measurement period or final determination of the values of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the consolidated statements of operations.

Goodwill and Acquired Intangible Assets

The Company records goodwill when consideration paid in a business acquisition exceeds the value of the net assets acquired. The Company’s estimates of fair value are based upon assumptions believed to be reasonable at that time but that are inherently uncertain and unpredictable. Assumptions may be incomplete or inaccurate, and unanticipated events or circumstances may occur, which may affect the accuracy or validity of such assumptions, estimates or actual results.

Goodwill is not amortized, but rather is tested for impairment annually or more frequently at the reporting unit level if facts and circumstances warrant a review. The Company has determined that there is a single reporting unit for the purpose of conducting this goodwill impairment assessment. The Company estimates the fair value of the reporting unit (based on the Company’s market capitalization) and compares this amount to the carrying value of the reporting unit (as reflected by the Company’s total stockholders’ equity). If the Company determines that the carrying value of the reporting unit exceeds its fair value, an impairment charge would be required. The Company’s annual goodwill impairment test is performed at November 30th of each year. To date, the Company has not identified any impairment

to goodwill.

Intangible assets acquired in a business combination are recorded at their estimated fair values at the date of acquisition. The Company amortizes acquired intangible assets over their estimated useful lives based on the pattern of consumption of the

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economic benefits or, if that pattern cannot be readily determined, on a straight-line basis. The Company reviews its intangible assets with definite lives for impairment when events or changes in circumstances indicate that the related carrying amount may not be recoverable. The details of the Company's intangible asset impairment assessment are included in Note 5 - Fair Value of Financial Instruments.

Software Development Costs

The Company accounts for its software and website development costs in accordance with the guidance in ASC 350-40, Internal-Use Software and ASC 350-50, Website Development Costs. The costs incurred in the preliminary stages of development are expensed as incurred. Once an application has reached the development stage, internal and external costs, if direct and incremental, are capitalized until the application is substantially complete and ready for its intended use, at which point such costs are amortized over the estimated useful life of the software. As of December 31, 2018 and December 31, 2017, the Company had capitalized $7.7 million and $6.8 million of costs associated with internal-use software, respectively. For the years ended December 31, 2018, 2017, and 2016, the Company recorded $1.1 million, $0.5 million, and $0.4 million of amortization expense related to capitalized internal-use software, respectively.

Purchased software costs that qualify for capitalization are accounted for in accordance with ASC 985, Software, Subtopic 20, Costs of Software to Be Sold, Leased, or Marketed ("ASC 985"). Purchased software represents software licenses purchased from third parties. Development costs for software to be sold externally incurred subsequent to the establishment of technological feasibility or if it meets the future alternative use criteria, but prior to the general release of the product, are capitalized and, upon general release, are amortized on a straight-line basis over the estimated useful life of the software. The asset associated with purchased software is included in acquired intangible assets, net in the consolidated balance sheets.

Advertising Expenses

The Company expenses advertising costs as incurred. During the years ended December 31, 2018, 2017, and 2016, the Company incurred approximately $17.0 million, $16.4 million, and $17.8 million of advertising expense, respectively, which is included in sales and marketing expense in the accompanying statements of operations.

Accounts Receivable

Accounts receivable are recorded at the invoiced amount. The allowance for doubtful accounts reflects the Company’s best estimate of the amount of probable credit losses in the Company’s existing accounts receivable. The Company specifically analyzes historical bad debts, the aging of the accounts receivable, creditworthiness, and current economic trends to evaluate the allowance for doubtful accounts. Past due balances are reviewed individually for collectability. Account balances are charged against the allowance for doubtful accounts after all means of collection have been exhausted, and the potential for recovery is considered remote. The allowance for doubtful accounts is recorded as a reduction in accounts receivable. The Company also maintains an allowance for sales returns and credits to customers for which the Company has the ability to estimate based upon historical experience. The allowance for sales returns and credits is recorded as a reduction in revenue.

The following is a rollforward of the Company's accounts receivable reserve and allowance (in thousands):

| | Balance Beginning of Period | Charged to Statement of Operations | Deductions (1) | Balance End of Period |
|---|---|---|---|---|
| Year ended December 31, 2018 | $ 994 | $ 227 | $ (329 ) | $ 892 |
| Year ended December 31, 2017 | $ 1,587 | $ (444 ) | $ (149 ) | $ 994 |
| Year ended December 31, 2016 | $ 139 | $ 1,462 | $ (14 ) | $ 1,587 |

(1) Deductions include actual accounts written-off, net of recoveries and credits issued.

Income Taxes

The Company provides for income taxes under the liability method. Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the

enacted tax rates in effect when the differences are expected to reverse. In certain jurisdictions, deferred tax assets are reduced by a valuation allowance to reflect the uncertainty associated with their ultimate realization. The Company accounts for uncertain tax positions recognized in the consolidated financial statements by prescribing a more-likely-than-not threshold for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return.

Due to a history of losses, the Company has provided a full valuation allowance against its deferred tax assets in the U.S. and in certain foreign jurisdictions that are in a deferred tax asset position for which the Company is uncertain as to their

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ultimate realization. This is more fully described in Note 12- Income Taxes. The ability to utilize these deferred tax assets may be restricted or eliminated by changes in the Company's ownership, changes in legislation, and other rules affecting the ability to offset future taxable income with losses or other tax attributes from prior periods. Future determinations on the need for a valuation allowance on the Company's net deferred tax assets will be made on a quarterly basis.

Segment Information

Operating segments are defined as components of an enterprise for which separate financial information is regularly evaluated by the chief operating decision maker (“CODM”), which is the Company’s chief executive officer, in deciding how to allocate resources and assess performance. The Company’s CODM evaluates the Company’s financial information and resources and assess the performance of these resources on a consolidated basis. The Company views its operations and manages its business in one operating segment. Since the Company operates in one operating segment, all required financial segment information can be found in the consolidated financial statements.

Stock-Based Compensation

The Company recognizes stock-based compensation as an expense in the financial statements using the estimated grant-date fair value over the individual award's requisite service period, which equals the vesting periods in all cases but for certain market-based awards. The Company uses the straight-line amortization method for recognizing stock-based compensation expense. The Company estimates the fair value of stock options on the date of grant using the Black-Scholes option-pricing model and the fair value of stock options and awards with market-based vesting conditions on the date of grant using a Monte Carlo simulation. These models require the use of highly subjective estimates and assumptions, including expected stock price volatility, expected term of an award, risk-free interest rate, and expected dividend yield. The grant date fair value of restricted stock units granted is based on the fair value of the underlying common stock on the date of grant.

Costs Associated with Exit Activities

The determination of when the Company accrues for employee involuntary termination benefits depends on whether the termination benefits are provided under an ongoing benefit arrangement or under a one-time benefit arrangement. The Company accounts for employee termination benefits that represent a one-time benefit in accordance with ASC 420, Exit or Disposal Cost Obligations ("ASC 420"). The Company accounts for ongoing benefit arrangements in accordance with ASC 712, Compensation-Nonretirement Postemployment Benefits. Other costs associated with exit activities include contract termination costs, including costs related to leased facilities to be abandoned or subleased, expensed in accordance with ASC 420.

Reclassifications

The Company adopted Accounting Standard Update ("ASU") 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (“ASU 2016-18”), effective January 1, 2018. Restricted cash is defined as cash and cash equivalents subject to contractual restrictions and not readily available for use. The Company applied this standard retrospectively by reclassifying restricted cash to be presented with cash and cash equivalents on the consolidated statement of cash flows. As of December 31, 2016, the restricted cash balance of $0.1 million related to a security deposit maintained for certain office space that was subleased to third parties. For the year ended December 31, 2018 and 2017, the Company did not have a restricted cash balance reported within the consolidated balance sheets.

The Company has reclassified certain prior period amounts in its consolidated statements of operations to conform to the current period presentation. The reclassification relates to separately presenting amortization of intangible assets previously included within general and administrative and sales and marketing. For the year ended December 31, 2017, the Company reclassified $0.5 million from general and administrative and $1.6 million from sales and marketing into the amortization of intangible assets caption within operating expenses. For the year ended December 31, 2016, the Company reclassified $0.3 million from general and administrative and $1.0 million from sales and marketing into the amortization of intangible assets caption within operating expenses.

The Company has reclassified certain prior period amounts in its consolidated balance sheets to conform to the current period presentation. The reclassification relates to separately presenting accrued compensation which was previously included in the accrued expenses and other current liabilities caption. As of December 31, 2017, the Company reclassified $9.9 million from accrued expenses and other current liabilities into the accrued compensation caption.

Recently Adopted Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Topic 606, which updated guidance and disclosure requirements for recognizing revenue. The new revenue recognition standard provides a five-step analysis of

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transactions to determine when and how revenue is recognized. The revenue standard is based on the principle that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The Company adopted this standard effective January 1, 2018 using the modified retrospective transition method. The Company recognized the cumulative effect of applying the new standard as an adjustment to the opening balance of retained earnings at the beginning of 2018. The comparative information for 2017 has not been restated and continues to be reported under the accounting standards in effect for the period presented. Refer to Note 3 - Revenue Recognition for the required disclosures related to the impact of adopting this standard and accounting for costs to obtain and fulfill a customer contract.

In March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (“ASU 2016-09”). The amendments in this ASU involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. On January 1, 2017, the Company adopted ASU 2016-09. In connection with the adoption of this standard, the Company changed its accounting policy to record actual forfeitures as they occur, rather than estimating forfeitures by applying a forfeiture rate. As this policy change was applied prospectively, prior periods have not been adjusted. As a result of adoption in 2017, the Company recorded an immaterial impact to retained earnings and additional paid in capital. The Company retrospectively adjusted the classification of excess tax benefits on the statement of cash flow from financing to operating; the effect was immaterial.

In October 2016, the FASB issued ASU 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory (“ASU 2016-16”). The purpose of ASU 2016-16 is to simplify the income tax accounting of an intra-entity transfer of an asset other than inventory and to record its effect when the transfer occurs. The guidance is effective for annual reporting periods beginning after December 15, 2017, including interim reporting periods within those annual reporting periods and early adoption is permitted. The Company adopted ASU 2016-16 effective January 1, 2018, which did not have a material impact on the consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, which requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents and amounts generally described as restricted cash or restricted cash equivalents. Entities will also be required to reconcile such total to amounts on the balance sheet and disclose the nature of the restrictions. The guidance is effective for annual reporting periods beginning after December 15, 2017 and interim periods within those fiscal years. The Company adopted ASU 2016-18 effective January 1, 2018, which did not have a material impact on the consolidated financial statements. The Company applied this standard retrospectively by reclassifying restricted cash to be presented with cash and cash equivalents on the consolidated statement of cash flows.

In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment ("ASU 2017-04"). The standard eliminates the second step in the goodwill impairment test which requires an entity to determine the implied fair value of the reporting unit’s goodwill. The standard is effective for annual and interim goodwill impairment tests conducted in fiscal years beginning after December 15, 2019, with early adoption permitted. The Company elected to early adopt ASU 2017-04 effective January 1, 2018, which did not have a material impact on the consolidated financial statements.

Recently Issued Accounting Pronouncements

In February 2016, the FASB issued ASU 2016-02, Leases ("ASU 2016-02"). ASU 2016-02 requires lessees to recognize the assets and liabilities on their balance sheet for the rights and obligations created by most leases and continue to recognize expenses on their income statements over the lease term. It will also require disclosures designed to give financial statement users information on the amount, timing, and uncertainty of cash flows arising from leases. The guidance is effective for annual reporting periods beginning after December 15, 2018 and interim periods within those fiscal years, with early adoption permitted. The Company will adopt the new standard effective January 1, 2019 on a modified retrospective basis and will not restate comparative periods. The Company is currently evaluating the effect of the standard on its consolidated financial statements and expects that upon adoption a material lease obligation and right to use asset will be recognized on its consolidated balance sheets. The Company's leases

primarily relate to office and data center space. Refer to Note 13 - Commitments and Contingencies for additional information related to the Company’s lease obligations.

In August 2018, the FASB issued ASU 2018-15, Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract. This standard aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The standard is effective for annual and interim periods beginning after December 15, 2019, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this standard on its consolidated financial statements.

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3. Revenue Recognition

On January 1, 2018, the Company adopted Topic 606 applying the modified retrospective method to all contracts that were not completed as of January 1, 2018. Where applicable, the Company utilized the practical expedient and reflected the aggregate effect of all contract modifications that occurred prior to adoption as they related to performance obligations (both satisfied and remaining) and determination and allocation of the transaction price. Under the modified retrospective method, results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with the applicable accounting in effect for those periods. The adoption of Topic 606 did not significantly impact the majority of the Company's offerings. Under the new guidance, the Company's revenue recognition associated with term licenses and software contracts with a minimum monthly royalty commitment is accelerated. Further, the Company has begun capitalizing certain incremental costs incurred in obtaining contracts with customers as an asset on the consolidated balance sheets. These costs were previously expensed in the period they were incurred. The Company recorded a $13.9 million increase to retained earnings as of January 1, 2018, due to the cumulative impact of adopting Topic 606 on revenue from contracts with customers. Upon adoption, trade accounts receivable, net increased $2.2 million and deferred revenue decreased $4.0 million. Prepaid expenses and other current assets increased $1.5 million and other assets increased by $6.6 million primarily related to the capitalization of sales commissions. Deferred tax liabilities increased by $0.4 million due to temporary differences between the accounting and tax carrying values of the capitalized commissions. The impact of adopting Topic 606 to revenues was an increase of $1.1 million for the year ended December 31, 2018.

Disaggregation of Revenue

The following table depicts disaggregated revenue for the year ended December 31, 2018, by type, customer type, sales channel, timing of revenue recognition, and geography (in thousands):

| | Year Ended December 31, 2018 | | |
|---|---|---|---|
| | Products | Services | Total |
| Customer type | | | |
| Consumer | $— | $95,185 | $95,185 |
| Business | 33,324 | 167,899 | 201,223 |
| Total | $33,324 | $263,084 | $296,408 |
| | | | |
| Sales channel | | | |
| Direct | $4,193 | $181,122 | $185,315 |
| Indirect | 29,131 | 81,962 | 111,093 |
| Total | $33,324 | $263,084 | $296,408 |
| | | | |
| Timing of revenue recognition | | | |
| Transferred at a point in time | $33,324 | $— | $33,324 |
| Transferred over time | — | 263,084 | 263,084 |
| Total | $33,324 | $263,084 | $296,408 |
| | | | |
| Geography | | | |
| United States | $14,741 | $234,474 | $249,215 |
| Other | 18,583 | 28,610 | 47,193 |
| Total | $33,324 | $263,084 | $296,408 |

Contract Assets and Liabilities

Contract assets are rights to consideration in exchange for goods or services that the entity has transferred to a customer when that right is conditional on something other than the passage of time. Contract assets are transferred to

accounts receivable once the rights become unconditional. The Company did not have contract assets as of December 31, 2018.

Contract liabilities (deferred revenue) primarily consist of billings and payments received in advance of revenue recognition. The Company primarily bills and collects payments from customers for its services in advance on a monthly and annual basis. The Company initially records fees associated with performance obligations delivered over time as deferred revenue and then recognizes revenue as performance obligations are satisfied. The Company classifies deferred revenue as

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current or noncurrent based on the timing revenue recognition. Changes in contract liabilities for the year ended December 31, 2018 are as follows (in thousands):

| | Deferred Revenue (Short-term) | Deferred Revenue (Long-term) |
|---|---|---|
| Balance as of January 1, 2018 | $ 96,243 | $ 24,273 |
| Increase, net | 25,310 | 4,878 |
| Balance as of December 31, 2018 | $ 121,553 | $ 29,151 |

For the year ended December 31, 2018, revenue recognized related to deferred revenue at January 1, 2018 was approximately $93.7 million. Additionally, for the year ended December 31, 2018, the Company recognized $14.0 million of revenue from deferred revenue related to the acquisition of Mozy on March 19, 2018.

On December 31, 2018, the Company had $160.5 million of remaining performance obligations. This amount does not include any variable consideration for sales or usage-based royalties. The Company expects to recognize 80.0% of its remaining performance obligations as revenue in the year ended December 31, 2019, 15.0% in the year ended December 31, 2020, and the remaining balance thereafter.

Accounts Receivable, Net

Accounts receivable, net, are amounts due from customers where there is an unconditional right to consideration. Unbilled receivables of $3.6 million and $3.9 million are included in this balance at January 1, 2018 and December 31, 2018, respectively. The payment of consideration related to these unbilled receivables is subjected only to the passage of time.

Contract Costs

The Company also considered Topic 606 subtopic 340-40, Other Assets and Deferred Costs - Contracts with Customers (“subtopic 340-40”). Prior to adoption of Topic 606, the Company expensed costs to obtain and fulfill contracts with customers as incurred. Under subtopic 340-40, the Company capitalizes incremental costs incurred in obtaining contracts with customers if the amortization period is greater than one year. For costs that the Company would have capitalized and amortized over one year or less, the Company has elected to apply the practical expedient and expense these contract costs as incurred. These costs consist primarily of commissions paid when contracts are signed. For the year ended December 31, 2018, the Company capitalized $7.5 million in costs to obtain contracts with customers, which are amortized on a straight-line basis over the period of benefit. The Company has defined the period of benefit to be the average customer life of six years. For the year ended December 31, 2018, the Company had amortization expense of $2.2 million related to deferred costs. Amortization expense is included in sales and marketing expense in the consolidated statements of operations. As of December 31, 2018, the Company has $2.7 million and $10.6 million in current and non-current deferred costs of obtaining contracts with customers, respectively.

Financial Statement Impact of Adopting Topic 606

The Company adopted Topic 606 using the modified retrospective method. The cumulative effect of applying the new guidance to all contracts with customers that were not completed as of January 1, 2018 was recorded as an adjustment to accumulated deficit as of the adoption date.

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The following table summarizes the effects of adopting Topic 606 on the Company's consolidated balance sheet as of December 31, 2018 (in thousands):

| | December 31, 2018 | | |
|---|---|---|---|
| | As reported under Topic 606 | Adjustments | Balances under Prior GAAP |
| Trade accounts receivable, net | $31,569 | $ (2,635) | $28,934 |
| Prepaid expenses and other current assets | 10,409 | (2,723) | 7,686 |
| Other assets | 13,876 | (10,587) | 3,289 |
| Accrued expenses and other current liabilities | 15,844 | (511) | 15,333 |
| Current portion of deferred revenue | 121,553 | 3,434 | 124,987 |
| Deferred revenue, net of current portion | 29,151 | 495 | 29,646 |
| Other long-term liabilities | 5,294 | (343) | 4,951 |
| Accumulated other comprehensive income | 1,650 | 203 | 1,853 |
| Accumulated deficit | (147,902) | (19,223) | (167,125) |

The following table summarizes the effects of adopting Topic 606 on the Company's consolidated income statement for the year ended December 31, 2018 (in thousands, except per share amounts):

| | Year Ended December 31, 2018 | | |
|---|---|---|---|
| | As reported under Topic 606 | Adjustments | Balances under Prior GAAP |
| Revenue | $296,408 | $ (1,122) | $295,286 |
| General and administrative | 50,547 | (595) | 49,952 |
| Sales and marketing | 85,637 | 5,328 | 90,965 |
| (Benefit) provision for income taxes | (13,347) | (512) | (13,859) |
| Net income (loss) | 7,562 | (5,343) | 2,219 |
| Net income (loss) per share - basic | 0.24 | (0.17) | 0.07 |
| Net income (loss) per share - diluted | 0.22 | (0.15) | 0.07 |

The adjustment to the general and administrative caption above relates to a sale of assets recorded in the twelve months ended December 31, 2018. The deferred revenue divested as part of the sale was $0.6 million higher under prior GAAP. This resulted in an adjustment between Topic 606 and prior GAAP related to the $0.6 million change in deferred revenue and gain (loss) on the sale of the assets.

The adoption of ASC 606 did not affect the Company's cash flows.

Revision of Prior Period Amounts

The Company has revised certain prior period amounts in its consolidated statements of operations. In connection with the Company’s adoption of Topic 606, the Company determined that product revenue has historically exceeded 10% of total revenue and therefore should have been previously stated separately from services revenue. While the Company believes the effect of this correction is immaterial to previously issued financial statements, the Company has revised the presentation to correctly present the services and products components of revenue and cost of revenue in the consolidated statements of operations for the years ended December 31, 2017 and December 31, 2016. The revision also includes presenting as a separate caption within costs of revenue, the amortization of intangible assets, which was previously included in the total cost of revenue. These revisions did not affect reported total revenue, total cost of revenue, loss from operations, net income or net income per share, the Company's cash flows; or any balance sheet line item.

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The effect of the revisions to the consolidated statements of operations for the year ended December 31, 2017 and December 31, 2016, is as follows (in thousands):

| | Year Ended December 31, 2017 | | | Year Ended December 31, 2016 | | |
|---|---|---|---|---|---|---|
| | As Previously Reported | Adjustments | As Revised | As Previously Reported | Adjustments | As Revised |
| Revenue: | | | | | | |
| Services | $ — | $ 207,403 | $ 207,403 | $ — | $ 186,087 | $ 186,087 |
| Product | — | 32,059 | 32,059 | — | 20,899 | 20,899 |
| Total revenue | 239,462 | — | 239,462 | 206,986 | — | 206,986 |
| Cost of revenue: | | | | | | |
| Services | — | 59,212 | 59,212 | — | 55,512 | 55,512 |
| Product | — | 2,676 | 2,676 | — | 2,793 | 2,793 |
| Amortization of intangible assets | — | 8,179 | 8,179 | — | 2,632 | 2,632 |
| Total cost of revenue | 70,067 | — | 70,067 | 60,937 | — | 60,937 |

4. Net Income (Loss) Per Share

Basic net income (loss) per share is calculated by dividing the net income (loss) by the weighted average number of common shares outstanding during the period. For the periods in which the Company reports net income, diluted net income per share is calculated by dividing net income by the sum of the weighted average number of common shares and potentially dilutive securities outstanding during the period using the treasury stock method. For the periods in which the Company reports a net loss, the dilutive effect of the Company's outstanding common stock equivalents are not included in the calculation of diluted loss per share as they would be anti-dilutive. The following table sets forth the computation of basic and diluted net income (loss) per share:

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | (In thousands, except per share data) | | |
| Numerator: | | | |
| Net income (loss) | $ 7,562 | $ (4,002) | $ (4,099) |
| Denominator: | | | |
| Weighted average common shares outstanding, basic | 31,036 | 27,779 | 27,029 |
| Effect of potential dilutive common shares | 2,636 | — | — |
| Weighted average shares outstanding, diluted | 33,673 | 27,779 | 27,029 |
| Basic net income (loss) per share | $ 0.24 | $ (0.14) | $ (0.15) |
| Diluted net income (loss) per share | $ 0.22 | $ (0.14) | $ (0.15) |

The Company has the ability and intent to settle the principal of the convertible senior notes (the "Convertible Notes"), issued in April 2017, in cash. The Company has included the dilutive effect of the Convertible Notes in the calculation of diluted net income per share for the year ended December 31, 2018, using the treasury stock method.

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The following options to purchase common shares, restricted stock units/awards and shares of common stock purchasable under the Company's 2017 Employee Stock Purchase Plan ("2017 ESPP") have been excluded from the computation of diluted net income (loss) per share because they had an anti-dilutive impact, or because they related to share-based awards that were contingently issuable, for which the applicable vesting conditions had not been satisfied (in thousands):

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| Options to purchase common shares (1) | — | 1,148 | 1,585 |
| Restricted stock units/awards | 57 | 1,696 | 1,853 |
| Total | 57 | 2,844 | 3,438 |

(1) The balances for the years ended December 31, 2018 and 2017 include shares purchasable under the Company's 2017 ESPP which were determined to be anti-dilutive.

5. Fair Value of Financial Instruments

Derivative Instruments

Non-designated Foreign Currency Contracts

The Company uses foreign currency forward contracts as part of our strategy to manage exposure related to Euro denominated intercompany monetary assets and liabilities. The Company has not designated these forward contracts as hedging instruments. Accordingly, the Company recorded the fair value of these contracts at the end of each reporting period in the consolidated balance sheets, with changes in the fair value recorded in earnings as other income (expense), net in the consolidated statements of operations. Cash flows from the settlement of these non-designated foreign currency contracts are reported in cash flows from investing activities. These currency forward contracts are entered into for periods consistent with currency transaction exposures, generally less than one year. At December 31, 2018 and 2017, we had outstanding contracts with a total notional value of $43.8 million and $47.8 million, respectively. The following table provides a quantitative summary of the fair value of derivative instruments not designated as hedging instruments as of December 31, 2018 and 2017 (in thousands):

| Description | Balance Sheet Classification | Fair Value | |
|---|---|---|---|
| | | December 31, 2018 | December 31, 2017 |
| | | (in thousands) | |
| Derivative Liabilities: | | | |
| Non-Designated Hedging Instruments | | | |
| Foreign currency contracts | Accrued expenses and other current liabilities | $ 195 | $ 439 |
| Total Derivative Liabilities | | $ 195 | $ 439 |

The following tables summarize the gains (losses) related to derivative instruments not designated as hedging instruments for the year ended December 31, 2018, 2017 and 2016 (in thousands):

| Description | Location in Statement of Operations | Years Ended December 31, | | |
|---|---|---|---|---|
| | | 2018 | 2017 | 2016 |
| Foreign currency contracts | Other income (expense), net | $2,832 | $(5,324) | $1,700 |

Other Fair Value Measurements

The Company applies the guidance in ASC 820, Fair Value Measurements and Disclosures, ("ASC 820"), which provides that fair value is based on 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 order to increase consistency and comparability in fair value measurements, ASC 820 establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

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Level 2: Other inputs that are observable directly or indirectly, such as quoted prices for similar assets and liabilities or market corroborated inputs.
Level 3: Unobservable inputs are used when little or no market data is available, which requires the Company to develop its own assumptions about how market participants would value the assets or liabilities. The fair value hierarchy gives the lowest priority to Level 3 inputs.
In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible in its assessment of fair value. The Company's assets and liabilities that are measured at fair value on a recurring basis, by level, within the fair value hierarchy are summarized as follows (in thousands):

| | December 31, 2018 | | | | December 31, 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| Assets: | | | | | | | | |
| Cash equivalents—money market funds | $156,200 | $ — | $ — | $156,200 | $96,295 | $ — | $ — | $96,295 |
| Total | $156,200 | $ — | $ — | $156,200 | $96,295 | $ — | $ — | $96,295 |
| Liabilities: | | | | | | | | |
| Foreign currency exchange contracts | — | 195 | — | 195 | — | 439 | — | 439 |
| Total | $— | $ 195 | $ — | $195 | $— | $ 439 | $ — | $439 |

The Company's investments in money market funds are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices. Our foreign currency exchange contracts are classified as Level 2 within the fair value hierarchy as they are valued using professional pricing sources for identical or comparable instruments, rather than direct observations of quoted prices in active markets. No assets or liabilities are classified as Level 3 within the fair value hierarchy.
The Company estimates the fair value of its Convertible Notes using quoted market prices in an inactive market on the last trading day of the reporting period and has been classified as Level 2 within the fair value hierarchy. The principal amount, carrying value of the Convertible Notes (the carrying value excludes the equity component of the Convertible Notes classified in equity) and related estimated fair value of the Company's Convertible Notes reported in the consolidated balance sheet as of December 31, 2018 and 2017 are as follows (in thousands):

| | December 31, 2018 | | | December 31, 2017 | | |
|---|---|---|---|---|---|---|
| | Principal | Carrying Value | Fair Value | Principal | Carrying Value | Fair Value |
| Convertible Notes | $143,750 | $118,305 | $168,287 | $143,750 | $111,819 | $174,548 |

The carrying amounts for cash and cash equivalents, accounts receivable, and accounts payable and accrued expenses approximate fair value because of their short maturities.
Non-Recurring Fair Value Measures
Certain non-financial assets, such as goodwill, intangible assets and property and equipment, are measured at fair value on a non-recurring basis and are adjusted to fair value only if an impairment charge is recognized. Such fair value measures are considered to be within the Level 3 valuation hierarchy due to the subjective nature of the unobservable inputs used.
During the year ended December 31, 2018, the Company recorded impairment charges totaling $0.7 million related to internally developed software costs which were no longer recoverable as the project was discontinued. The Company recorded the impairment charge in the cost of revenue, research and development, sales and marketing, and general and administrative captions in the consolidated statements of operations.
During the year ended December 31, 2017, the Company recorded impairment charges totaling $1.0 million related to capitalized software projects that were discontinued. The Company recorded the impairment charge in the research and development caption in the consolidated statements of operations. Additionally, during the year ended December 31, 2017, the Company recorded impairment charges totaling $0.4 million related to intangible assets whose carrying values were assessed to be unrecoverable. Of the total impairment charges, $0.2 million was recorded in the cost of revenue caption in the consolidated statements of operations related to an impairment of developed technology intangible asset, and $0.2 million was recorded in

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the sales and marketing caption in the consolidated statements of operations related to an impairment of customer relationship intangible asset.

6. Acquisitions

Acquisition-Related Expenses

In the twelve months ended December 31, 2018, 2017 and 2016 acquisition-related expenses were $6.3 million, $3.9 million, $4.5 million, respectively. Acquisition-related expenses have been included primarily in general and administrative expenses in the consolidated statements of operations. The Company's current year acquisition costs relate to the acquisition of Mozy and the prior year acquisition costs primarily relate to the acquisitions of certain assets of Datacastle, DoubleTake, and EVault.

2018 Acquisitions

Mozy

On February 12, 2018, the Company entered into a definitive Master Acquisition Agreement ("Agreement") with EMC Corporation (“EMC”), Mozy and Dell Technologies, Inc. Pursuant to the Agreement, on March 19, 2018, the Company completed the acquisition of all of the issued and outstanding capital stock of Mozy, a cloud backup service for consumers and businesses, and certain related business assets owned by EMC or its affiliates, for a purchase price of $144.6 million in cash, net of cash acquired. The purchase price was funded with cash on hand and funds available under the Company’s Revolving Credit Facility (refer to Note 16 - Borrowings and Credit Arrangements). In connection with the acquisition of Mozy, the Company negotiated a transition services agreement to cover certain consulting, technology and engineering services for up to eighteen months post close. The acquisition of Mozy has been accounted for as a business combination and the Company has recorded the assets acquired and liabilities assumed at their respective fair values as of the acquisition date.

The following tables summarize the final purchase price allocation (in thousands):

| Fair value of consideration transferred: | |
|---|---|
| Cash, net of cash acquired | $144,597 |
| Fair value of total acquisition consideration | $144,597 |

| Fair value of assets acquired and liabilities assumed: | |
|---|---|
| Accounts receivable | $1,629 |
| Prepaid expenses and other current assets | 872 |
| Property and equipment | 7,169 |
| Other long-term assets | 242 |
| Intangible assets | 96,400 |
| Goodwill | 74,753 |
| Total assets acquired | 181,065 |
| Accounts payable | (141) |
| Accrued liabilities | (417) |
| Deferred revenue | (19,740) |
| Deferred tax liability | (16,170) |
| Net assets acquired | $144,597 |

The Company engaged a third-party valuation firm to assist in the valuation of intangible assets consisting of customer relationships, developed technology and the Mozy trade name as well as in the valuation of deferred revenue and property and equipment. The fair values of the remaining Mozy assets and liabilities noted above approximate their carrying values at March 19, 2018.

The Company believes the goodwill related to the acquisition was a result of the ability of the Company to leverage its technology in the broader market, as well as offering cross-selling market exposure opportunities. Goodwill is not deductible for tax purposes as this acquisition was a stock purchase.

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The significant intangible assets identified in the purchase price allocation discussed above include customer relationships, developed technology, and trade names which are amortized over their estimated useful lives based on the pattern of consumption of the economic benefits or, if that pattern cannot be readily determined, on a straight-line basis. Customer relationships represent the underlying relationships with certain customers to provide ongoing services for products sold. To value the customer relationship asset, the Company utilized the income approach, specifically a discounted cash-flow method known as the excess earnings method. Developed technology consists of products that have reached technological feasibility and trade names represent acquired company and product names. The developed technology intangible was valued using a relief from royalty method, which considers both the market approach and the income approach. The trade name intangible was valued using the replacement cost/lost profits methodology. The following table presents the estimated fair values and useful lives of the identifiable intangible assets acquired and risk-adjusted discount rates used in the valuation:

| | Amount | Weighted Average Useful Life | Risk-Adjusted Discount Rates used in Valuation |
|---|---|---|---|
| | (in thousands) | (in years) | |
| Developed technology | $ 8,700 | 2 | 12.5% |
| Customer relationships | 87,200 | 7 | 16.5 - 17.5% |
| Trade names | 500 | 2 | 12.5% |
| Total identifiable intangible assets | $ 96,400 | | |

For the year ended December 31, 2018, the operating results of Mozy, which are included in the Company's consolidated statements of operations since the date of acquisition, include $48.5 million of Mozy subscription revenue. Mozy subscription revenue does not include revenue associated with Mozy customers that have transitioned to Carbonite branded offerings. The Company has determined that disclosing the amount of Mozy related expenses included in the consolidated statements of operations is impracticable, as certain operations of Mozy were integrated into the operations of the Company.

Pro Forma Financial Information (unaudited)

The following unaudited pro forma information presents the consolidated results of operations of the Company and Mozy for the years ended December 31, 2018 and December 31, 2017 as if the acquisition of Mozy had been completed on January 1, 2017. These pro forma consolidated financial results have been prepared for comparative purposes only and include certain adjustments that reflect pro forma results of operations, such as increased amortization for the fair value of acquired intangible assets, fair value adjustment for deferred revenue, additional annual interest expense resulting from interest on the Revolving Credit Facility to finance the acquisition of Mozy, reversal of depreciation expense resulting from the application of fair value measurement to acquired property and equipment and adjustments relating to the tax effect of combining the Carbonite and Mozy businesses.

The unaudited pro forma results do not reflect any operating efficiencies or potential cost savings which may result from the consolidation of the operations of the Company and Mozy. Accordingly, these unaudited pro forma results are presented for informational purposes only and are not necessarily indicative of the results of operations that actually would have been achieved had the acquisition occurred as of January 1, 2017 nor are they intended to represent or be indicative of future results of operations (in thousands):

| | Years Ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| Pro forma revenue | $311,416 | $306,567 |
| Pro forma net income (loss) | $10,700 | $(2,885 ) |
| Pro forma net income (loss) per common share: | | |
| Basic | $0.34 | $(0.10 ) |
| Diluted | $0.32 | $(0.10 ) |

2017 Acquisitions

Datacastle

On August 14, 2017, the Company entered into an asset purchase agreement with Datacastle to purchase all the assets associated with Datacastle's cloud data backup, caching and analytics software and services for data protection purposes, for a



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purchase price of $9.6 million in cash at closing. The acquisition of Datacastle has been accounted for as a business combination and the Company has recorded the assets acquired and liabilities assumed at their respective fair values as of the acquisition date. Pro forma information has not been presented, as the operating results of Datacastle are not material.

The following tables summarize the final purchase price allocation (in thousands):

| Fair value of consideration transferred: | |
|---|---|
| Cash | $9,600 |
| Fair value of total acquisition consideration | $9,600 |

| Fair value of assets acquired and liabilities assumed: | |
|---|---|
| Accounts receivable | $298 |
| Prepaid expenses and other current assets | 90 |
| Intangible assets | 3,440 |
| Goodwill | 6,267 |
| Total assets acquired | 10,095 |
| Accrued liabilities | (175 ) |
| Deferred revenue | (320 ) |
| Net assets acquired | $9,600 |

The Company engaged a third-party valuation firm to assist in the valuation of intangible assets and deferred revenue. The fair values of the remaining Datacastle assets and liabilities noted above approximate their carrying values at August 14, 2017. In connection with the acquisition of Datacastle, goodwill was recognized as the excess purchase price over the fair value of net assets acquired. The goodwill recorded in connection with this transaction is primarily related to the ability to leverage existing sales and marketing capacity and customer base with respect to the acquired product, as well as revenue and cash flow projections associated with future technologies. Goodwill from the acquisition of Datacastle is included within the Company’s one reporting unit and will be included in the annual review for impairment. The goodwill is fully deductible for tax purposes.

The significant intangible assets identified in the purchase price allocation include developed technology and customer relationships, which are amortized over their respective useful lives on a straight line basis which approximates the underlying cash flows. To value the developed technology asset, the Company utilized the income approach, specifically a discounted cash-flow method known as the excess earnings method. The Company utilized the distributor earnings approach to derive the fair value of the customer relationships. The following table presents the fair values and useful lives of the identifiable intangible assets acquired and risk-adjusted discount rates used in the valuation:

| | Amount | Weighted Average Useful Life | Risk-Adjusted Discount Rates used in Valuation |
|---|---|---|---|
| | (in thousands) | (in years) | |
| Developed technology | $ 2,550 | 7 | 11.0% |
| Customer relationships | 890 | 10 | 13.0% |
| Total identifiable intangible assets | $ 3,440 | | |

DoubleTake

On January 31, 2017, the Company completed the acquisition of all the outstanding capital stock of DoubleTake for a purchase price of $65.9 million, which was comprised of $59.7 million in cash paid at closing, net of cash acquired, 332,326 shares of our common stock with a fair value of $5.7 million and the working capital payment of $0.5 million. The working capital settlement was paid in June 2017. DoubleTake develops, sells, and supports affordable software that allows IT organizations of all sizes to move, manage, protect, and recover workloads across any distance and any combination of physical and virtual server environments. DoubleTake’s products and services are marketed and sold worldwide through their direct sales force and a network of business partners and distributors. In connection with the acquisition of DoubleTake, the Company negotiated a transition services agreement ("TSA") to cover certain consulting, technology and accounting services for up to nine months post close. The Company incurred $1.2 million

under the TSA. The acquisition of DoubleTake has been accounted

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for as a business combination and the Company has recorded the assets acquired and liabilities assumed at their respective fair values as of the acquisition date.

The following tables summarize the final purchase price allocation (in thousands):

| Fair value of consideration transferred: | |
|---|---|
| Cash, net of cash acquired | $59,740 |
| Fair value of equity instruments | 5,733 |
| Working capital payment | 458 |
| Fair value of total consideration | $65,931 |

| Fair value of assets acquired and liabilities assumed: | |
|---|---|
| Accounts receivable | $6,058 |
| Prepaid and other current assets | 158 |
| Property and equipment | 428 |
| Other long-term assets | 42 |
| Intangible assets | 36,700 |
| Goodwill | 49,473 |
| Total assets acquired | 92,859 |
| Accounts payable | (636 ) |
| Accrued liabilities | (2,156 ) |
| Deferred revenues | (9,100 ) |
| Deferred tax liability | (14,918 ) |
| Other non-current liabilities | (118 ) |
| Net assets acquired | $65,931 |

The Company engaged a third-party valuation firm to assist in the valuation of intangible assets consisting of developed technology, customer relationships, and the DoubleTake trade name as well as in the valuation of deferred revenue. The fair values of the remaining DoubleTake assets and liabilities noted above approximate their carrying values at January 31, 2017.

In connection with the acquisition of DoubleTake, goodwill of $49.5 million was recognized for the excess purchase price over the fair value of the net assets acquired. The Company believes the goodwill recorded in connection with this transaction is primarily related to the investment value of the future enhancements of our product offering and solutions offering. Goodwill from the acquisition of DoubleTake is included within the Company’s one reporting unit and will be included in the annual review for impairment. Goodwill is not deductible for tax purposes as this acquisition was a stock purchase.

The significant intangible assets identified in the purchase price allocation discussed above include developed technology, trade names and customer relationships, which are amortized over their estimated useful lives based on the pattern of consumption of the economic benefits or, if that pattern cannot be readily determined, on a straight-line basis. To value the developed technology asset, the Company utilized the income approach, specifically a discounted cash-flow method known as the multi-period excess earnings method. The trade name intangible was valued using a relief from royalty method, which considers both the market approach and the income approach. Customer relationships represent the underlying relationships with certain customers to provide ongoing services for products sold. The Company utilized the replacement cost/lost profits methodology to derive the fair value of the customer relationships. The following table presents the fair values and useful lives of the identifiable intangible assets acquired and risk-adjusted discount rates used in the valuation:

| | Amount | Weighted Average Useful Life | Risk-Adjusted Discount Rates used in Valuation |
|---|---|---|---|
| | (in thousands) | (in years) | |
| Developed technology | $ 29,900 | 5 | 13.5% |
| Customer relationships | 4,900 | 6 | 12.0% |
| Trade names | 1,900 | 8 | 12.0% |
| | $ 36,700 | | |

Total identifiable intangible assets

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Pro Forma Financial Information (unaudited)

The following unaudited pro forma information presents the consolidated results of operations of the Company and DoubleTake for the year ended December 31, 2017 and 2016 as if the acquisition of DoubleTake had been completed on January 1, 2016. These pro forma consolidated financial results have been prepared for comparative purposes only and include certain adjustments that reflect pro forma results of operations, such as increased amortization for the fair value of acquired intangible assets, fair value adjustment for deferred revenue, elimination of interest expense with a promissory note due to the parent company, and adjustments relating to the tax effect of combining the Carbonite and DoubleTake businesses.

The unaudited pro forma results do not reflect any operating efficiencies or potential cost savings which may result from the consolidation of the operations of the Company and DoubleTake. Accordingly, these unaudited pro forma results are presented for informational purposes only and are not necessarily indicative of the results of operations that actually would have been achieved had the acquisition occurred as of January 1, 2016, nor are they intended to represent or be indicative of future results of operations (in thousands, except per share data):

| | Years Ended December 31, | |
|---|---|---|
| | 2017 | 2016 |
| Pro forma revenue | $242,743 | $242,348 |
| Pro forma net loss | $(4,037) | $(13,671) |
| Pro forma net loss per common share: | | |
| Basic | $(0.15) | $(0.50) |
| Diluted | $(0.15) | $(0.50) |

2016 Acquisition

EVault

On January 13, 2016, the Company completed the acquisition of the North American cloud-based business continuity and disaster recovery assets of EVault and the acquisition of the assets used in the European Union operations of EVault was completed on March 31, 2016. The Company acquired EVault to offer business continuity and disaster recovery solutions designed for SMBs and small enterprises. The acquisition of EVault has been accounted for as a business combination and, in accordance with ASC 805, the Company has recorded the assets acquired and liabilities assumed at their respective fair values as of the acquisition dates.

In connection with the acquisition of EVault, the Company negotiated a transition services agreement ("EVault TSA") that provides a credit to be used against future services provided under the terms of the agreement. The Company estimated the fair value of the EVault TSA credit to be $2.4 million and accounted for it as a reduction in consideration transferred in the purchase price allocation. The EVault TSA credit was recorded in prepaid expenses and other current assets on the consolidated balance sheet as of the acquisition date. The EVault TSA credit was fully expensed in 2016, and as such, there is no remaining balance of the EVault TSA credit on the consolidated balance sheet as of December 31, 2018. The following tables summarize the final purchase price allocation (in thousands):

| Fair value of consideration transferred: | |
|---|---|
| Cash | $14,000 |
| Fair value of prepaid EVault TSA | (2,375) |
| Fair value of total acquisition consideration | $11,625 |

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| Fair value of assets acquired and liabilities assumed: | |
|---|---|
| Prepaid expenses | $1,330 |
| Property and equipment | 6,776 |
| Intangible assets | 9,150 |
| Other long-term assets | 564 |
| Goodwill | 989 |
| Total assets acquired | 18,809 |
| Deferred revenue | (6,830 ) |
| Accrued liabilities | (354 ) |
| Net assets acquired | $11,625 |

The significant intangible assets identified in the purchase price allocation discussed above include developed technology, trade names and customer relationships, which are amortized over their respective useful lives on a straight-line basis. Developed technology consists of products that have reached technological feasibility and trade names represent acquired company and product names. To value the developed technology asset, the Company utilized the income approach, specifically a discounted cash-flow method known as the multi-period excess earnings method. The trade name intangible was valued using a relief from royalty method, which considers both the market approach and the income approach. Customer relationships represent the underlying relationships with certain customers to provide ongoing services for products sold. The Company utilized the replacement cost/lost profits methodology to derive the fair value of the customer relationships.

The following table presents the fair values and useful lives of the identifiable intangible assets acquired and risk-adjusted discount rates used in the valuation:

| | Amount | Weighted Average Useful Life | Risk-Adjusted Discount Rates used in Valuation |
|---|---|---|---|
| | (in thousands) | (in years) | |
| Developed technology | $ 5,650 | 4 | 15% |
| Customer relationships | 2,500 | 6 | 14% |
| Trade names | 1,000 | 7 | 14% |
| Total identifiable intangible assets | $ 9,150 | | |

Pro Forma Financial Information (unaudited)

The following unaudited pro forma information presents the combined results of operations of the Company and EVault for the twelve months ended December 31, 2015 as if the acquisition of EVault had been completed on January 1, 2015. These pro forma consolidated financial results have been prepared for comparative purposes only and include certain adjustments that reflect pro forma results of operations, such as increased amortization for the fair value of acquired intangible assets, fair value adjustments (step-downs) for property, plant and equipment and deferred revenue, reversal of revenues and costs directly attributable to assets and products not acquired, and adjustments relating to the tax effect of combining the Company and EVault businesses.

The unaudited pro forma results do not reflect any operating efficiencies or potential cost savings which may result from the consolidation of the operations of the Company and EVault.

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Accordingly, these unaudited pro forma results are presented for informational purposes only and are not necessarily indicative of the results of operations that actually would have been achieved had the acquisition occurred as of January 1, 2015, nor are they intended to represent or be indicative of future results of operations (in thousands):

| | Year Ended December 31, 2015 |
|---|---|
| Revenue | $220,403 |
| Net loss | $(102,376) |
| | |
| Basic and diluted net loss per share | $(3.77) |
| Weighted-average number of common shares used in computing basic and diluted net loss per share | 27,187,910 |

The pro forma financial information shown above includes a nonrecurring adjustment of $3.3 million, to eliminate transaction costs directly attributable to the acquisition incurred by the Company for the year ended December 31, 2015, in arriving at the pro forma net loss shown above.

7. Goodwill and Acquired Intangible Assets

The following is a rollforward of our goodwill balance (in thousands):

| | December 31, | |
|---|---|---|
| | 2018 | 2017 |
| Balance at beginning of fiscal period | $80,958 | $23,728 |
| Goodwill acquired | 74,753 | 55,740 |
| Goodwill divested | (29) | (27) |
| Effect of foreign exchange rates | (596) | 1,517 |
| Balance at end of fiscal period | $155,086 | $80,958 |

Purchased intangible assets related to the Company's acquisitions and purchased software that form the basis of the Company's products consist of the following (in thousands):

| | | December 31, 2018 | | | December 31, 2017 | | |
|---|---|---|---|---|---|---|---|
| | Weighted-Average Estimated Useful Life (in years) | Gross Carrying Value | Accumulated Amortization | Net Carrying Value | Gross Carrying Value | Accumulated Amortization | Net Carrying Value |
| Technology-related | 4.4 | $59,018 | $ 26,551 | $32,467 | $46,833 | $ 12,504 | $34,329 |
| Customer relationships | 6.8 | 96,997 | 13,398 | 83,599 | 11,295 | 3,361 | 7,934 |
| Trade names | 2.8 | 3,752 | 1,855 | 1,897 | 3,677 | 946 | 2,731 |
| Non-compete agreements | 0.0 | — | — | — | 230 | 230 | — |
| Total | 4.7 | $159,767 | $ 41,804 | $117,963 | $62,035 | $ 17,041 | $44,994 |

The Company recorded amortization expense of $28.1 million, $10.3 million and $3.9 million for the years ended December 31, 2018, 2017 and 2016, respectively. Technology-related intangible assets consist of developed technology acquired and purchased software, which represents software licenses purchased from third parties. Amortization relating to technology-related assets is recorded within a separate line within cost of revenue and amortization of customer relationships, trade names and non-compete agreements is recorded within a separate line within operating expenses.

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Future estimated amortization expense of acquired intangibles is as follows (in thousands):

| | |
|---|---|
| 2019 | $27,253 |
| 2020 | 22,406 |
| 2021 | 21,254 |
| 2022 | 15,352 |
| 2023 | 13,919 |
| Thereafter | 17,779 |
| Total | $117,963 |

On October 3, 2017, the Company entered into a license and distribution agreement to be utilized in future product offerings. As consideration for granting the license, the Company agreed to pay $7.0 million in three separate milestone payments. The Company paid $1.25 million upon transfer of all licensed materials in October 2017, $1.25 million related to progress made in January 2018, and $4.5 million upon completion and acceptance of certain deliverables in July 2018. Under ASC 985, these costs are capitalized as incurred and amortized over their estimated useful life on a straight-line basis. As the product was released in late September 2018, the amortization of these development costs began in October 2018 on a straight-line basis over the estimated useful life of the software, which was determined to be seven years.

8. Property and Equipment

Property and equipment consists of the following (in thousands):

| | December 31, | |
|---|---|---|
| | 2018 | 2017 |
| Computer equipment | $56,204 | $46,113 |
| Software | 3,668 | 3,211 |
| Furniture and fixtures | 3,013 | 2,344 |
| Leasehold improvements | 14,428 | 11,163 |
| Internal-use software | 7,745 | 6,793 |
| Appliances | 1,731 | 1,131 |
| Total property and equipment | 86,789 | 70,755 |
| Less accumulated depreciation and amortization | (52,688 ) | (41,965 ) |
| Property and equipment, net | $34,101 | $28,790 |

Depreciation and amortization expense was $13.7 million, $11.5 million, and $12.0 million for the years ended December 31, 2018, 2017, and 2016, respectively.

9. Accrued Expenses

Accrued expenses consist of the following (in thousands):

| | December 31, | |
|---|---|---|
| | 2018 | 2017 |
| Accrued tax liabilities | $4,588 | $2,280 |
| Accrued consulting and professional fees | 3,103 | 2,162 |
| Accrued sales and marketing | 1,606 | 1,124 |
| Accrued facilities | 1,807 | 1,002 |
| Accrued interest | 980 | 898 |
| Accrued restructuring | — | 688 |
| Derivative liability | 195 | 439 |
| Accrued other expenses | 3,565 | 3,190 |
| Total accrued expenses | $15,844 | $11,783 |

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10. Stockholders' Equity
Share Repurchase Program
On May 11, 2015, the Company's Board of Directors authorized a $20.0 million share repurchase program, which was subsequently increased to $30.0 million, effective from May 15, 2015 through May 15, 2018. On May 15, 2018, the share repurchase program was not renewed by the Company. On November 19, 2018, the Company's Board of Directors authorized a $50.0 million share repurchase program in lieu of the previously expired program. Share repurchases are made from time-to-time in the open market, in privately negotiated transactions or otherwise, in accordance with applicable securities laws and regulations. The timing and amount of any share repurchases are determined by the Company's management based on an evaluation of market conditions, the trading price of the stock, and other factors.
The Company made the following repurchases under the programs during years ended December 31, 2018, 2017, and 2016:

| | December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| | (total cost, in thousands) | | |
| Number of shares repurchased | 809,921 | 767,400 | 574,118 |
| Average repurchase price per share | $26.55 | $19.50 | $7.81 |
| Total cost | $21,501 | $14,964 | $4,481 |

At December 31, 2018, approximately $28.5 million remained available under the Company's share repurchase program.
Secondary Offering
On July 23, 2018, 4,765,157 shares of common stock, with a par value $0.01 per share, were issued and sold in a public offering by the Company. Additionally, the underwriters exercised their full 30-day option on August 16, 2018 and an additional 819,485 shares were issued and sold. Proceeds of $199.3 million were recognized by the Company, net of underwriting discounts and commissions and offering expenses paid. The net proceeds recognized less the par value of the shares issued were recorded within additional paid-in capital in the Company's consolidated balance sheets.
11. Stock-based Awards
The Company's 2005 Stock Incentive Plan (the "2005 Plan") provided for granting of incentive stock options, non-qualified options, restricted stock, or other awards to the Company's employees, officers, directors, and outside consultants up to an aggregate of 3,601,551 shares of the Company's common stock. In conjunction with the effectiveness of the 2011 Equity Award Plan (the "2011 Plan"), the Company's Board of Directors voted that no further stock options or other equity-based awards would be granted under the 2005 Plan.
The 2011 Plan provides for the issuance of stock options, restricted stock, restricted stock units, and other stock-based awards to the employees, officers, directors, and consultants of the Company or its subsidiaries. In connection with the approval of the 2011 Plan, the Company reserved 1,662,000 shares of common stock for issuance thereunder. On January 1st of each year, beginning on January 1, 2012, the number of shares reserved under the 2011 Plan increased or will increase by the lesser of 1,500,000 shares, 4.0% of the outstanding shares of common stock and common stock equivalents, or another amount determined by the Company's Board of Directors. As of December 31, 2018, 2,569,335 shares of common stock were available for future grant under the 2011 Plan.
Stock-based awards granted to employees generally vest over a four-year period, and, in the case of stock options, expire ten years from the date of grant. Certain awards provide for accelerated vesting if there is a change of control, as defined in the 2005 or 2011 Plan, as applicable. The Company has generally granted stock options at exercise prices not less than the fair market value of its common stock on the date of grant.
Stock Options
The Company generally estimates the fair value of stock options on the date of grant using the Black-Scholes option-pricing model. This model requires the use of highly subjective estimates and assumptions, including expected stock price volatility, expected term of an award, risk-free interest rate, and expected dividend yield. The Company

did not grant any stock options in the years ended December 31, 2018 and 2017.

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The assumptions used to estimate the fair value of the stock options granted for the year ended December 31, 2016 were as follows:

| | December 31, 2016 |
|---|---|
| Weighted-average exercise price | $ 8.95 |
| Weighted-average grant-date fair value | $ 4.03 |
| Black-Scholes Assumptions | |
| Risk-free interest rate | 1.93 % |
| Expected dividend yield | — |
| Expected volatility | 44 % |
| Expected term (in years) | 6.10 |

Risk-Free Interest Rate

The Company bases the risk-free interest rate that it uses in the option valuation model on U.S. Treasury zero-coupon issues with remaining maturities similar to the expected term of the options.

Expected Dividend Yield

The Company has not paid, and does not anticipate paying, cash dividends on shares of common stock; therefore, the expected dividend yield is assumed to be zero in the option valuation model.

Expected Volatility

The Company estimates the expected volatility of its common stock at the date of grant based on the historical volatility of comparable public companies over the option's expected term as well as its own stock price volatility.

Expected Term

The expected term is estimated using the "simplified method." The simplified method is based on the average of the vesting tranches and the contractual life of each grant.

The following table summarizes stock option activity under stock incentive plans for the year ended December 31, 2018:

| | Number of Shares | Weighted-Average Exercise Price per Share | Weighted-Average Remaining Contractual Life (in years) | Aggregate Intrinsic Value (in thousands) (1) |
|---|---|---|---|---|
| Outstanding at December 31, 2017 | 834,679 | $ 11.45 | 5.99 | $ 11,391 |
| Granted | — | — | | |
| Exercised | (109,496) | 11.24 | | |
| Cancelled | (6,372 ) | 11.91 | | |
| Outstanding at December 31, 2018 | 718,811 | $ 11.48 | 4.99 | $ 9,904 |
| Exercisable as of December 31, 2018 | 690,100 | $ 11.44 | 4.94 | $ 9,537 |

(1) The aggregate intrinsic value is calculated as the positive difference between the exercise price of the underlying stock options and the market value of the Company's common stock on December 31, 2018 and December 31, 2017 as reported on the NASDAQ Stock Market.

The total intrinsic value of options exercised during the years ended December 31, 2018, 2017, and 2016 was approximately $2.1 million, $4.2 million, and $1.8 million, respectively. As of December 31, 2018, there was approximately $0.1 million of unrecognized stock-based compensation cost related to unvested stock options that is expected to be recognized over a weighted-average period of 0.34 years.

Restricted Stock Units

The Company recognizes non-cash compensation expense over the vesting term of restricted stock units. The fair value is measured based upon the number of units and the closing price of the Company's common stock underlying such units on the dates of grant. Upon vesting and settlement, each restricted stock unit entitles the holder to receive

one share of common stock.



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The following table summarizes all restricted stock unit activity for the year ended December 31, 2018:

| | Number of Shares | Weighted Average Grant Date Fair Value |
|---|---|---|
| Unvested restricted stock units as of December 31, 2017 | 1,418,261 | $ 15.12 |
| Restricted stock units granted | 711,978 | 27.98 |
| Restricted stock units vested | (562,551 ) | 14.42 |
| Restricted stock units cancelled | (110,612 ) | 21.94 |
| Unvested restricted stock units as of December 31, 2018 | 1,457,076 | $ 21.16 |

As of December 31, 2018, there was approximately $22.4 million of unrecognized stock-based compensation cost related to unvested restricted stock units that is expected to be recognized over a weighted-average period of 2.18 years.

Restricted Stock Awards

The Company grants restricted stock awards to members of the Board of Directors annually. The fair value is measured based upon the number of units and the closing price of the Company’s common stock underlying such units on the dates of grant. Awards to directors vest on the earlier of the first anniversary of the date of grant or the Company's Annual Meeting. The following table summarizes restricted stock award activity for the year ended December 31, 2018:

| | Number of Shares | Weighted Average Grant Date Fair Value |
|---|---|---|
| Unvested restricted stock awards as of December 31, 2017 | 58,279 | $ 19.60 |
| Restricted stock awards granted | 28,777 | 34.90 |
| Restricted stock awards vested (restriction lapsed) | (52,260 ) | 19.67 |
| Restricted stock awards forfeited | — | — |
| Unvested restricted stock awards as of December 31, 2018 | 34,796 | $ 32.15 |

As of December 31, 2018, there was approximately $0.4 million of unrecognized stock-based compensation cost related to unvested restricted stock units that is expected to be recognized over a weighted-average period of 0.48 years.

Equity Awards with Market-Based Vesting Conditions

During the years ended December 31, 2018, 2017, and 2016, the Company granted 151,580, 168,884 and 325,000 restricted stock units with market-based vesting conditions to certain key executives, respectively. These restricted stock units contain both market-based and service vesting conditions. The market-based vesting conditions are achieved if the closing price of the Company's common stock meets or exceeds a specified target price for 20 consecutive trading days. The awards are subject to additional service vesting which typically occurs in four equal quarterly installments over the one-year period beginning on the date the market-based vesting conditions are met. This vesting is subject to the recipient's continued service to the Company through the applicable vesting date.

The Company estimated the fair value and derived service period of the restricted stock units with market-based vesting conditions on the date of grant using a Monte-Carlo simulation. The model requires the use of subjective estimates and assumptions, including expected volatility, risk-free interest rate and dividend yield.

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The grant-date stock price and assumptions used to estimate the derived service period and fair value of the equity awards with market-based vesting conditions were as follows:

| | As of February 14, 2018 | As of August 4, 2017 | As February 10, 2017 | As of February 1, 2016 |
|---|---|---|---|---|
| Grant-date stock price | $26.53 | $21.15 | $19.15 | $8.95 |
| Assumptions | | | | |
| Expected volatility | 39 % | 39 % | 42 % | 40 % |
| Risk-free interest rate | 2.39 % | 1.44 % | 1.47 % | 1.01 % |
| Expected dividend yield | — % | — % | — % | — % |

The Company recognizes the stock-based compensation expense on equity awards with market-based vesting conditions in the consolidated statements of operations over the requisite service period. The achievement of certain market-based vesting conditions may result in the acceleration of recognizing stock-based compensation expense compared to the original valuation.

The following table summarizes equity awards with market-based vesting conditions activity for the year ended December 31, 2018:

| | Restricted Stock Units with Market-Based Vesting Conditions | Weighted Average Grant Date Fair Value |
|---|---|---|
| Unvested market-based vesting awards as of December 31, 2017 | 218,884 | $ 13.26 |
| Market-based vesting awards granted | 151,580 | 19.57 |
| Market-based vesting awards vested | (223,588 ) | 15.40 |
| Market-based vesting awards forfeited | (16,397 ) | 18.42 |
| Unvested market-based vesting awards as of December 31, 2018[1] | 130,479 | $ 16.28 |

(1) In addition to the unvested market-based vesting awards above, there were 250,000 vested market-based vesting options outstanding and exercisable as of December 31, 2018 and December 31, 2017, respectively. As of December 31, 2018, these options had an exercise price of $14.44, a remaining contractual term of 5.92 years, and an intrinsic value of $2.7 million.

As of December 31, 2018, there was approximately $0.4 million of unrecognized stock-based compensation cost related to unvested awards with market-based vesting conditions that are expected to be recognized over a weighted-average period of 0.26 years.

For the year ended December 31, 2018 and 2017, the total fair value of restricted stock awards, restricted stock units, performance-based stock awards on the date vested was $25.4 million, and $17.8 million, respectively.

Stock-based Compensation Expense

Stock-based compensation is reflected in the consolidated statements of operations as follows for the years ended December 31, 2018, 2017, and 2016 (in thousands):

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| Cost of revenues | $1,545 | $1,061 | $807 |
| Research and development | 3,292 | 1,969 | 868 |
| General and administrative | 9,697 | 7,827 | 6,161 |
| Sales and marketing | 3,073 | 1,885 | 1,064 |
| Total | $17,607 | $12,742 | $8,900 |

Employee Stock Purchase Plan

On May 18, 2017, the Company registered 600,000 shares pursuant to the 2017 Employee Stock Purchase Plan ("2017 ESPP") on a Form S-8. Under this plan eligible employees may purchase shares of the Company's common stock, subject to certain limitations, at the lesser of 85% of the beginning or ending withholding period fair market value as defined in the 2017

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ESPP. There are two six-month withholding periods in each fiscal year. As of December 31, 2018, rights to acquire 420,314 shares of common stock were available for issuance under the 2017 ESPP.

12. Income Taxes

On December 22, 2017, the United States enacted tax reform legislation through the Tax Cuts and Jobs Act ("Tax Act"), which significantly changed the existing U.S. tax laws. The Tax Act includes a reduction in the U.S. corporate tax rate from 34% to 21%, a transition from a worldwide tax system to a modified territorial tax system, new taxes on certain foreign-sourced earnings, limitations on the deductibility of interest expense and executive compensation, as well as other changes.

In response to the Tax Act, the SEC staff issued Staff Accounting Bulletin No. 118 ("SAB 118") which allows registrants to record provisional amounts during a measurement period, not to extend beyond one year from the enactment date. Pursuant to SAB 118, the Company has completed the accounting for the tax effects of all of the provisions of the Tax Act within the required measurement period.

The Company remeasured all deferred tax assets and liabilities as of December 31, 2017, based on the provisions of the Tax Act, which include a reduction in the federal statutory tax rate from 34% to 21%. The impact of the remeasurement to the net deferred tax asset is a reduction of $8.9 million, which is fully offset by changes in the pre-existing valuation allowance. For the year ended December 31, 2017, the Company recorded a benefit of $0.2 million related to the Federal Alternative Minimum Tax ("AMT") credit, which is now refundable under the Tax Act.

In regard to the Tax Act's one-time tax on unrepatriated foreign earnings, the Company has performed an analysis and has determined that the Company does not have a liability as the Company has a net deficit of unrepatriated foreign earnings. The federal impacts of the Global Intangible Low-taxed Income ("GILTI") provision, the changes in the disallowed officers' compensation deductions and the changes in the deductibility of meals and entertainment are fully offset by net operating losses in 2018.

The domestic and foreign components of loss before (benefit) provision for income taxes were as follows (in thousands):

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| Domestic | $(11,895) | $(14,171) | $(1,911) |
| Foreign | 6,110 | (3,508) | (805) |
| Total loss before (benefit) for income taxes | $(5,785) | $(17,679) | $(2,716) |

The components of the (benefit) provision for income taxes are as follows (in thousands):

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| Current tax provision: | | | |
| Federal | $108 | $(395) | $90 |
| State | 163 | (24) | 219 |
| Foreign | 3,007 | 2,134 | 1,089 |
| Total current provision | 3,278 | 1,715 | 1,398 |
| Deferred tax benefit: | | | |
| Federal | (12,671) | (12,514) | — |
| State | (3,348) | (1,906) | 10 |
| Foreign | (606) | (972) | (25) |
| Total deferred benefit | (16,625) | (15,392) | (15) |
| Total (benefit) provision for income taxes | $(13,347) | $(13,677) | $1,383 |

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A reconciliation of our income tax (benefit) provision to the statutory federal tax rate is as follows:

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| U.S. federal income tax rate | 21.0 % | 34.0 % | 34.0 % |
| Change in the valuation allowance | 222.9 | 83.8 | (43.9) |
| Nondeductible stock-based compensation | 49.5 | 21.5 | 0.7 |
| State taxes, net of federal benefit | 8.4 | 5.9 | 1.6 |
| Foreign rate differential | (8.8 ) | (11.2) | (30.9) |
| U.S. foreign income inclusion | (33.1 ) | — | — |
| Income tax credits | 33.5 | 6.9 | 41.5 |
| Provision for tax reserves | (8.8 ) | 0.7 | (31.6) |
| Non-deductible compensation | (28.6 ) | (8.2 ) | (14.1) |
| Meals and entertainment | (4.2 ) | (1.2 ) | (2.4 ) |
| Transaction costs | (14.6 ) | (3.7 ) | (2.8 ) |
| Change in federal rate | — | (50.1) | — |
| Withholding taxes | (7.1 ) | (0.7 ) | — |
| Other | 0.6 | (0.3 ) | (3.0 ) |
| Effective income tax rate | 230.7 % | 77.4 % | (50.9)% |

The Company recorded a (benefit) provision for income taxes of $(13.3) million, $(13.7) million and $1.4 million for the years ended December 31, 2018, 2017, and 2016, respectively. For the year ended December 31, 2018, the Company's tax benefit was primarily driven by valuation allowance release and foreign income taxes. For the year ended December 31, 2017, the Company's tax benefit was primarily driven by valuation allowance release, foreign income taxes, and refundable AMT.

The components of the Company's deferred tax assets and liabilities are as follows (in thousands):

| | Years Ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| Deferred tax assets: | | |
| Net operating loss carryforwards | $26,572 | $27,792 |
| Research and development tax credit carryforwards | 7,928 | 6,280 |
| Deferred revenue | 4,733 | 3,957 |
| Stock compensation | 2,972 | 2,339 |
| Other | 6,871 | 7,304 |
| Total deferred tax assets | 49,076 | 47,672 |
| Valuation allowance for deferred tax assets | (12,291 ) | (28,273 ) |
| Total deferred tax assets, net of valuation allowance | 36,785 | 19,399 |
| Deferred tax liabilities: | | |
| Amortization | (22,638 ) | (9,146 ) |
| Convertible debt | (6,445 ) | (7,948 ) |
| Depreciation | (3,696 ) | (1,508 ) |
| Deferred costs | (2,955 ) | — |
| Other | (1,869 ) | (1,942 ) |
| Total deferred tax liabilities | (37,603 ) | (20,544 ) |
| Net deferred tax liabilities | $(818 ) | $(1,145 ) |

As of December 31, 2018, the Company had U.S. federal, state and foreign net operating loss carryforwards of $110.0 million, $75.9 million, and $2.3 million, respectively. The federal net operating loss carryforwards will expire at various dates beginning in 2027 through 2038. State net operating loss carryforwards will expire at various dates beginning in 2020 through 2038. At December 31, 2018, the Company had federal and state research and development tax credit carryforwards available

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to reduce future income taxes payable of $6.9 million and $3.8 million, respectively. These credits will expire at various dates beginning in the year 2025 through 2038. As of December 31, 2018, the Company also had refundable federal AMT credits of approximately $0.2 million.

Management has evaluated the positive and negative evidence bearing upon the realizability of its deferred tax assets. As required by the provisions of ASC 740, Income Taxes ("ASC 740"), management has determined that it is not more-likely-than-not that the tax benefits related to the federal, state and foreign deferred tax assets will be realized for financial reporting purposes. Accordingly, the federal, state and certain foreign deferred tax assets have been fully reserved at December 31, 2018 and 2017. The valuation allowance decreased approximately $16.0 million during the year ended December 31, 2018 primarily due to the partial release of U.S. valuation allowance as a result of a net deferred tax liability recorded in the acquisition of Mozy. The U.S. net deferred tax liability primarily relates to non-tax deductible intangible assets recognized in the financial statements which generate a deferred tax liability. The net deferred tax liability established is estimated to be a source of income to utilize previously unrecognized deferred tax assets in the U.S. Therefore, we have recorded a tax benefit of $16.2 million for the release of U.S. valuation allowance related to the previously unrecognized deferred tax assets in the U.S. The U.S. maintains a valuation allowance on the overall U.S. net deferred tax asset as it is deemed more likely than not the U.S. net deferred tax asset will not be realized. Furthermore, the 2018 change in valuation allowance is also impacted by a deferred tax liability related to the adoption of Topic 606. The valuation allowance decreased approximately $24.7 million during the year ended December 31, 2017 due primarily to the partial release of U.S. valuation allowance as a result of a net deferred tax liability recorded in the acquisition of DoubleTake.

Future changes in Company ownership may limit the amount of net operating loss carryforwards and research and development credit carryforwards that can be utilized annually to offset future taxable income and taxes, respectively. In general, an ownership change, as defined by Section 382 of the Internal Revenue Code of 1986, as amended, results from transactions increasing the ownership of certain shareholders or public groups in the stock of a corporation by more than 50 percentage points over a three-year period. Based upon the Company's analysis as of December 31, 2018, there was no ownership change experienced during 2018.

Unrecognized Tax Benefits

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in thousands):

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| Unrecognized tax benefits, beginning of year | $(3,700) | $(4,108) | $(3,231) |
| Additions based on tax positions related to the current year | (473) | (673) | (943) |
| Additions for tax positions of prior years | (58) | — | (14) |
| Reductions for tax positions of prior years | 7 | 1,081 | 80 |
| Unrecognized tax benefits, end of year | $(4,224) | $(3,700) | $(4,108) |

The Company accounts for uncertain tax positions under the recognition and measurement criteria of ASC 740. For those tax positions for which it is more likely than not that a tax benefit will be sustained, we record the largest amount of tax benefit with a greater than 50% likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. If we do not believe that it is not more likely than not that a tax benefit will be sustained, no tax benefit is recognized. As of December 31, 2018, the Company had a total amount of unrecognized tax benefits of $4.2 million, of which $0.1 million represents the amount of unrecognized tax benefits that, if recognized, would favorably affect the effective income tax rate in future periods. The difference between the total amount of unrecognized tax benefits and the amount that would impact the effective tax rate consists of items that, if recognized, would result in a corresponding increase in the valuation allowance.

The Company recognizes interest and penalties related to uncertain tax positions as a component in income tax expense. As of December 31, 2018, the Company had no accrued interest or penalties related to uncertain tax positions and no amounts have been recognized in the Company's consolidated statements of operations. The statute of limitations for assessment by the Internal Revenue Service ("IRS") and state tax authorities is open for tax years ending December 31, 2015, 2016, 2017 and 2018, although carryforward attributes that were generated prior to tax year 2014 may still be adjusted upon examination by the IRS or state tax authorities if they either have been or will be

used in a future period. The statute of limitations for assessments by foreign taxing authorities is generally not open for years prior to 2013, although carryforward attributes that were generated prior to tax year 2013 may still be adjusted upon examinations.

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The Company is subject to U.S. federal income tax and various state and local taxes in both domestic and foreign jurisdictions. In the normal course of business, the Company is subject to examination by taxing authorities within these jurisdictions. The Company is not currently under examination in any domestic or foreign jurisdiction.
The Company does not reasonably expect that the unrecognized tax benefit will change significantly within the next twelve months.
As of December 31, 2018, a deferred tax liability has not been established for approximately $16.2 million of cumulative undistributed earnings of non-U.S. subsidiaries, which are expected to be permanently reinvested in operations outside the U.S. Determination of the unrecognized deferred tax liability on unremitted earnings is not practical due to uncertainty regarding the remittance structure, the mix of earnings and earnings for profit pools in the year of remittance, and overall complexity of the calculation.

13. Commitments and Contingencies

Operating Leases

The Company leases facilities under leases that expire at varying dates through 2029. Certain of these leases contain renewal options and require the Company to pay operating costs, including property taxes, insurance, and maintenance.
The Company has lease agreements to rent office and data center space. The Company also has data center colocation agreements in place to rent colocation space.
The terms of several of the Company's leases include escalating rent and free rent periods. Accordingly, the Company recorded a deferred rent liability related to the free rent and escalating rent payments, such that rent is being recognized on a straight-line basis over the terms of the leases. Rent expense was $8.8 million, $8.9 million and $8.1 million for the fiscal years ended December 31, 2018, 2017 and 2016, respectively. At December 31, 2018 and 2017, $4.5 million and $4.7 million is included in accrued expenses and other current liabilities and other long-term liabilities related to the deferred rent, respectively. Future non-cancellable minimum lease payments under all operating leases as of December 31, 2018, are as follows (in thousands):

| Years Ended December 31, | Office Leases | Data Center Leases (1) | Total |
|---|---|---|---|
| 2019 | $4,194 | $4,833 | $9,027 |
| 2020 | 3,975 | 4,434 | 8,409 |
| 2021 | 3,888 | 2,133 | 6,021 |
| 2022 | 3,713 | 833 | 4,546 |
| 2023 | 3,655 | 70 | 3,725 |
| Thereafter | 5,183 | — | 5,183 |
| Total | $24,608 | $12,303 | $36,911 |

(1) Certain amounts in the table above relating to colocation leases for the Company's servers include usage based charges in addition to base rent.

Other Non-Cancellable Commitments

As of December 31, 2018, the Company had non-cancellable commitments to vendors primarily consisting of hosted software, consulting, advertising, marketing and broadband services contracts through 2021, as follows (in thousands):

| Years Ended December 31, | Commitments |
|---|---|
| 2019 | $ 18,069 |
| 2020 | 1,069 |
| 2021 | 125 |
| Total | $ 19,263 |

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Litigation

On February 27, 2017, a non-practicing entity named Realtime Data LLC ("Realtime Data") filed a lawsuit against the Company in the U.S. District Court for the Eastern District of Texas, alleging that the Company's cloud storage services infringe upon certain patents held by Realtime Data. Realtime Data's complaint against the Company sought damages in an unspecified amount and injunctive relief. On December 19, 2017, the United States District Court for the Eastern District of Texas transferred the case to the United States District Court of Massachusetts. Realtime Data has filed patent suits against several other companies around the country, and one or more of the asserted patents are currently in various stages of other litigations and/or United States Patent and Trademark Office ("USPTO") post-grant proceedings. The Company has requested the Court stay the case pending USPTO post-grant proceedings as to some of the asserted patents. No trial date has been set. The Company intends to defend itself vigorously. The Company has not accrued a loss contingency related to this matter because litigation related to a non-practicing entity is inherently unpredictable. Although a loss is reasonably possible, an unfavorable outcome is not considered by management to be probable at this time and the Company remains unable to reasonably estimate a possible loss or range of loss associated with this litigation.

The Company is from time to time subject to various other legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. The Company routinely assesses its current litigation and/or threatened litigation as to the probability of ultimately incurring a liability, and records its best estimate of the ultimate loss if reasonably possible to estimate, in situations where the Company assesses the likelihood of loss as probable. While the outcome of these other claims cannot be predicted with certainty, management does not believe that the outcome of any of these other legal matters will have a material adverse effect on the Company's condensed consolidated financial statements.

14. Restructuring

In October 2017, the Company initiated a restructuring program ("2017 Plan") to streamline operations and reduce operating costs. The 2017 plan was completed in the fourth quarter of 2018. The Company incurred restructuring charges totaling $1.8 million related to employee severance under the 2017 plan. In the third quarter of 2018, the Company incurred restructuring expenses related to lease exit charges from a data center facility that was exited during the quarter, as the Company determined to consolidate select data center space.

The following table summarizes the restructuring program activity for the year ended December 31, 2018 and 2017 (in thousands):

| | Employee Severance and Related Costs | Facilities Related Costs | Total |
|---|---|---|---|
| Accrued restructuring as of December 31, 2016 | $ — | $ — | $ — |
| Charges | 1,047 | — | 1,047 |
| Cash payments | (359) | — | (359) |
| Accrued restructuring as of December 31, 2017 | 688 | — | 688 |
| Charges | 803 | 467 | 1,270 |
| Cash payments | (1,460) | (467) | (1,927) |
| Non-cash and other adjustments | (31) | — | (31) |
| Accrued restructuring as of December 31, 2018 | $ — | $ — | $ — |

In 2016, the Company recorded restructuring charges of $0.9 million. These charges were associated with the reorganization and consolidation of certain operations and the disposal of certain assets during 2016, due to the EVault acquisition. These restructuring activities were completed in March 2016.

Restructuring-related expenses have been included in restructuring charges within the Company's consolidated statements of operations. The accrual for restructuring-related expenses have been included in accrued expenses and other current liabilities within the Company's consolidated balance sheets.

15. Retirement Plan

The Company has a 401(k) defined contribution savings plan for its employees who meet certain employment status and age requirements. The plan allows participants to contribute a portion of their annual compensation on a pre-tax basis. Effective January 1, 2012, the Company elected to make a matching contribution of up to 4% of each employee's wages. For the periods

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ending December 31, 2018, 2017 and 2016, the total expense for the Company's matching contributions to the plan was $3.0 million, $2.5 million, and $1.8 million, respectively.

16. Borrowings and Credit Arrangements

Revolving Credit Facility

On March 19, 2018, the Company entered into a Revolving Credit Facility which provides revolving credit financing of up to $130.0 million, including a $10.0 million sub-limit for letters of credit and a $10.0 million sub-limit for swingline loans. The commitments under the Revolving Credit Facility may be increased by up to an additional $100.0 million plus an additional unlimited amount so long as the Company does not exceed a specified pro forma secured net leverage ratio, in either case provided the existing or additional lenders are willing to make such increased commitments and subject to other terms and conditions.

The Revolving Credit Facility matures on the earlier of March 20, 2023 or, 91 days prior to the maturity of the Company's outstanding Convertible Notes, to the extent the same have not been repurchased, redeemed or otherwise refinanced as permitted under the Revolving Credit Facility. Borrowings bear interest at a variable rate equal to LIBOR plus an applicable margin as defined in the credit agreement. The Revolving Credit Facility is secured by substantially all of the Company's assets and contains customary affirmative and negative covenants, including, among others, certain limitations on the incurrence of indebtedness, guarantees and liens, the making of investments, acquisitions and dispositions, the payment of dividends and the repurchase of capital stock and the repayment, redemption or amendment of subordinated debt.

During the year ended December 31, 2018, the Company repaid $90.0 million of its outstanding borrowings under the Revolving Credit Facility. As of December 31, 2018, the Company had no outstanding borrowings under the facility. The Revolving Credit Facility also contains certain financial covenant ratios related to leverage and interest coverage that the Company must maintain.

Convertible Senior Notes

On April 4, 2017, the Company issued, in a private offering, $143.8 million aggregate principal amount of Convertible Notes. The Convertible Notes accrue interest at 2.5% per year, payable semiannually in arrears on April 1 and October 1 of each year. The Convertible Notes will mature on April 1, 2022, unless earlier repurchased, redeemed or converted.

The conversion rate for the Convertible Notes is initially 38.7034 shares of Company's common stock per $1,000 principal amount of Convertible Notes, which is equivalent to an initial conversion price of approximately $25.84 per share of common stock. Prior to January 1, 2022, the Convertible Notes will be convertible by the holders only upon satisfaction of the following conditions and during following periods:

1. During any calendar quarter commencing after the calendar quarter ending on September 30, 2017 (and only during such calendar quarter), if the last reported sale price of the Company's 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;
2. 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 notes for each trading day of the Measurement Period was less than 98% of the product of the last reported sale price of our common stock and the conversion rate on each such trading day;
3. If the Company calls any or all of the notes for redemption at any time prior to the close of business on the second scheduled trading day immediately preceding the redemption date; and
4. Upon the occurrence of certain specified corporate events.

On or after January 1, 2022 until the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their notes at any time. The Company may satisfy any conversion obligations by paying or delivering, as the case may be, cash, shares of its common stock or a combination of cash and shares of its common stock, at the Company's election in the manner and subject to the terms and conditions provided in the indenture governing the Convertible Notes.

The Company may redeem for cash all or any portion of the Convertible Notes, at its option, on or after April 5, 2020 if the last reported sale price of the Company's common stock has been at least 130% of the conversion price then in effect for at least 20 trading days (whether or not consecutive), during any 30 consecutive trading day period ending on the trading day

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immediately preceding the date on which the Company provides notice of redemption at a redemption price equal to 100% of the principal amount of the Convertible Notes to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date.

The Company received $138.7 million in proceeds from the issuance of the Convertible Notes, net of debt issuance costs and the discounts to the initial purchasers. The Company used $39.2 million of the proceeds to repay all amounts outstanding under its revolving credit facility and $15.0 million of the proceeds to repurchase shares of its common stock from purchasers of Convertible Notes in privately negotiated transactions effected through one or more of the initial purchasers or their affiliates conducted concurrently with the pricing of the Convertible Notes. The remaining proceeds will be used for general corporate purposes, including potential acquisitions.

In accordance with ASC 470-20, Debt with Conversion and Other Options, the Company separated the Convertible Notes into liability and equity components. The carrying amount of the liability component was calculated by measuring the fair value of a similar liability that does not have an associated convertible feature. The carrying amount of the equity component representing the conversion option was determined by deducting the fair value of the liability component from the par value of the Convertible Notes as a whole. The excess of the principal amount of the liability component over its carrying amount ("debt discount") is amortized to interest expense over the term of the Convertible Notes. The equity component is included in the additional paid-in-capital portion of stockholders' equity on the Company's consolidated balance sheet, and is not remeasured as long as it continues to meet the conditions for equity classification.

In addition, the debt issuance costs and debt discount are allocated between the liability and equity components in proportion to the allocation of the proceeds. The issuance costs and discount allocated to the liability component are capitalized as a reduction of the principal amount of the Convertible Notes payable on the Company's balance sheet and amortized, using the effective-interest method, as additional interest expense over the term of the Convertible Notes.

The issuance costs and discount allocated to the equity component are recorded as a reduction to additional paid-in capital. The Convertible Notes consisted of the following (in thousands):

| | Years Ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| Liability component: | | |
| Principal | $143,750 | $143,750 |
| Less: debt issuance costs | (573) | (720) |
| Less: debt discount | (24,872) | (31,211) |
| Net carrying amount | $118,305 | $111,819 |
| Equity component | $31,451 | $31,451 |

For the years ended December 31, 2018 and 2017, the Company incurred total interest expense associated with the Convertible Notes as follows (in thousands):

| | Years Ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| Interest expense related to contractual interest coupon | $3,594 | $2,655 |
| Interest expense related to accretion of the discount | 6,340 | 4,434 |
| Interest expense related to debt issuance costs | 146 | 102 |
| Total | $10,080 | $7,191 |

As of December 31, 2018, the net carrying value of the Convertible Notes was $118.3 million, which is net of unamortized debt issuance costs of $0.6 million. The effective interest rate on the Convertible Notes, including amortization of debt issuance costs and accretion of the discount, is 8.7%. At December 31, 2018, the conversion option value of the Convertible Notes does not exceed their principal amount since the closing market price of the Company's common stock does not exceed the conversion rate. As of December 31, 2018, the Convertible Notes were not convertible.

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17. Geographic Data

As more fully described in Note 2 - Summary of Significant Accounting Policies, the Company operates in one operating segment. Revenue by geographic region was based on physical location of the operations recording the sale. Revenues by geographic region are presented as follows (in thousands):

| | Years Ended December 31, | |
|---|---|---|
| | 2018 | 2017 |
| United States | $249,215 | $209,161 |
| International | 47,193 | 30,301 |
| Total | $296,408 | $239,462 |

For the year ended December 31, 2016, revenues by geographic region were not disclosed as revenue outside the United States did not exceed 10% of total revenue. No individual country other than the United States accounts for 10% or more of revenues in the years ended December 31, 2018, 2017 and 2016. Revenue included in the "International" caption above primarily relates to the Company's operations in Europe.

The Company does not disclose geographic information for long-lived assets, excluding deferred tax assets, goodwill and intangible assets. Long-lived assets, excluding deferred tax assets, goodwill and intangible assets, located outside the United States do not exceed 10% of total assets.

18. Subsequent Events

On February 7, 2019, the Company entered into an agreement and plan of merger to acquire Webroot. The Company will acquire all of the issued and outstanding capital stock of Webroot, a leading cybersecurity company, for $618.5 million in cash, which will be adjusted with respect to cash, debt, transaction expenses and working capital. The consummation of the merger is subject to certain closing conditions (excluding a financing condition) and also includes customary termination provisions for both Webroot and the Company, including if the merger has not been consummated by May 8, 2019, which date is subject to extension in certain circumstances with respect to regulatory clearance. The merger agreement also contains representations, warranties, and covenants by the parties that are customary for a transaction of this nature. The acquisition is expected to be consummated in the first quarter of 2019.

Concurrently with the execution of the merger agreement, the Company entered into a financing commitment letter (the "Commitment Letter") for (i) a seven-year senior secured term loan facility of $550.0 million (the "Term Loan Facility") and (ii) a five-year senior secured revolving credit facility (the "Revolving Facility" and, together with the Term Loan Facility, the "Facilities"). Upon execution of the Revolving Facility, the Company intends to terminate its previously executed Revolving Credit Facility entered into on March 19, 2018. The Company will fund the transaction with existing cash and the proceeds of borrowing under the Facilities. The Facilities will be subject to certain customary representations, warranties and covenants. The funding of the Facilities is subject to the Company's compliance with customary terms and conditions precedent as set forth in the Commitment Letter, including the execution and delivery of definitive documentation consistent with the Commitment Letter and the substantially simultaneous consummation of the merger on terms consistent with the merger agreement.

19. Quarterly Information (Unaudited)

Quarterly results of operations are as follows (in thousands, except per share amounts):

| | For the Three Months Ended | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Dec. 31, 2018 | Sept. 30, 2018 | June 30, 2018 | March 31, 2018 | Dec. 31, 2017 | Sept. 30, 2017 | June 30, 2017 | March 31, 2017 |
| Statements of Operations Data: | | | | | | | | |
| Revenue | $76,966 | $77,682 | $77,734 | $64,026 | $61,692 | $61,637 | $59,034 | $57,099 |
| Gross profit | $54,780 | $55,854 | $54,677 | $45,714 | $44,881 | $44,047 | $40,723 | $39,744 |
| Income (loss) from operations | $2,558 | $4,316 | $(281 ) | $(2,926 ) | $555 | $(1,094 ) | $(4,653 ) | $(6,873 ) |
| Net income (loss) | $719 | $586 | $(5,687 ) | $11,944 | $(1,614 ) | $(3,603 ) | $(6,380 ) | $7,595 |
| Basic net income (loss) per share | $0.02 | $0.02 | $(0.20 ) | $0.42 | $(0.06 ) | $(0.13 ) | $(0.23 ) | $0.27 |
| Diluted net income (loss) per share | $0.02 | $0.02 | $(0.20 ) | $0.40 | $(0.06 ) | $(0.13 ) | $(0.23 ) | $0.27 |

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## ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

## ITEM 9A. CONTROLS AND PROCEDURES

### Disclosure 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 December 31, 2018. 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 December 31, 2018, 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.

### Management’s Annual Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act as a process designed by, or under the supervision of our principal executive and principal financial officers and effected by our Board of Directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and disposition of our assets;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that our receipts and expenditures are being made only in accordance with authorizations of our management and Board of Directors; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on our financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2018. Management based its assessment on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework) ("COSO").

Based on management’s assessment of Carbonite, Inc., management has concluded that our internal control over financial reporting was effective as of December 31, 2018.

Deloitte & Touche LLP, an independent registered public accounting firm, has issued a report on our internal control over financial reporting as of December 31, 2018, which is included below.

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Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the quarter ended December 31, 2018 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the stockholders and the Board of Directors of Carbonite, Inc.

Opinion on Internal Control over Financial Reporting

We have audited the internal control over financial reporting of Carbonite, Inc. and subsidiaries (the "Company") as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements as of and for the year ended December 31, 2018, of the Company and our report dated February 28, 2019, expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the Company’s change in method of accounting for revenue from contracts with customers and costs to obtain a contract.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control over Financial Reporting

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Deloitte & Touche LLP

Boston, Massachusetts
February 28, 2019

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ITEM 9B. OTHER INFORMATION

None.

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## PART III

### ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Except as set forth below with respect to the Company's Code of Business Conduct and Ethics, the information required by this item will be set forth in the sections entitled "Board of Directors, Corporate Governance & Related Matters", "Section 16(a) Beneficial Ownership Reporting Compliance", "Executive Officers" and "Criteria for Procedures Director Nominations" of our definitive proxy statement to be filed with the SEC in connection with our 2019 annual meeting of stockholders (the "Proxy Statement"), which is expected to be filed not later than 120 days after the end of our fiscal year ended December 31, 2018, and is incorporated in this Annual Report by reference.

We have adopted a Code of Business Conduct and Ethics that applies to all of our directors, officers and employees, including our principal executive officer and principal financial officer. The Code of Business Conduct and Ethics is posted on our website at http://investor.carbonite.com/governance.cfm.

We intend to satisfy the disclosure requirement under Item 5.05 of Form 8-K regarding an amendment to, or waiver from, a provision of this Code of Business Conduct and Ethics by posting such information on our website, at the address and location specified above and, to the extent required by the listing standards of The NASDAQ Global Market, by filing a Current Report on Form 8-K with the SEC, disclosing such information.

### ITEM 11. EXECUTIVE COMPENSATION

The information required by this item will be set forth in the sections entitled "Compensation Discussion and Analysis", "Compensation Committee Interlocks and Insider Participation" and "Report of the Compensation Committee of the Board of Directors on Executive Compensation" of our Proxy Statement and is incorporated in this Annual Report by reference.

### ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this item will be set forth in the sections entitled "Security Ownership of Certain Beneficial Owners and Management" and "Equity Compensation Plan Information" of our Proxy Statement and is incorporated in this Annual Report by reference.

### ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information, if any, required by this item will be set forth in the sections entitled "Certain Relationships And Related Transactions" and "Board of Directors, Corporate Governance & Related Matters - Independence of our Board of Directors" of our Proxy Statement and is incorporated in this Annual Report by reference.

### ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this item will be set forth in the section entitled "Audit-Related Matters" of our Proxy Statement and is incorporated in this Annual Report by reference.

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PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a)(1) Financial Statements

See Index to Consolidated Financial Statements on page 44 of this Annual Report, which is incorporated into this Item by reference.

(a)(3) Exhibits

See Exhibit Index to this Annual Report, which is incorporated into this Item by reference. Each management contract or compensatory plan or arrangement required to be filed has been identified.

(b) Exhibits

See Exhibit Index to this Annual Report, which is incorporated into this Item by reference.

(c) Financial Statement Schedules

No schedules are submitted because they are not applicable, not required or because the information is included in the Consolidated Financial Statements or Notes to Consolidated Financial Statements.

ITEM 16. FORM 10-K SUMMARY

None.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

CARBONITE, INC.

Dated: February 28, 2019 By: /s/ Mohamad Ali
Mohamad Ali
Chief Executive Officer

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Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant in the capacities and on the dates indicated.

| Signature | Title | Date |
|---|---|---|
| /s/ Mohamad Ali<br>Mohamad Ali | Chief Executive Officer and Director<br>(Principal Executive Officer) | February 28, 2019 |
| /s/ Anthony Folger<br>Anthony Folger | Chief Financial Officer<br>(Principal Financial Officer) | February 28, 2019 |
| /s/ Cassandra Hudson<br>Cassandra Hudson | Chief Accounting Officer (Principal Accounting Officer) | February 28, 2019 |
| /s/ Stephen Munford*<br>Stephen Munford | Chairman of the Board | February 28, 2019 |
| /s/ Marina Levinson*<br>Marina Levinson | Director | February 28, 2019 |
| /s/ Charles Kane*<br>Charles Kane | Director | February 28, 2019 |
| /s/ Todd Krasnow*<br>Todd Krasnow | Director | February 28, 2019 |
| /s/ Linda Connly*<br>Linda Connly | Director | February 28, 2019 |
| /s/ Scott Daniels*<br>Scott Daniels | Director | February 28, 2019 |
| /s/ David Friend*<br>David Friend | Director | February 28, 2019 |

February 28, 2019

*By: /s/ Mohamad Ali
*Mohamad Ali Attorney-in-Fact

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EXHIBIT INDEX

| Exhibit No. | Description |
|---|---|
| 2.1 | Master Acquisition Agreement by and among Carbonite, Inc., EMC Corporation, Mozy, Inc. and Dell Technologies Inc. dated February 12, 2018. (Filed as Exhibit 2.1 to Form 8-K filed with the Securities and Exchange Commission on March 19, 2018 and incorporated herein by reference). |
| 3.1 | Amended and Restated Certificate of Incorporation of Carbonite, Inc. (Filed as Exhibit 3.1 to Amendment No. 2 to Registrant's Registration Statement on Form S-1/A filed with the Securities and Exchange Commission on July 13, 2011, and incorporated by reference.) |
| 3.2 | Amended and Restated By-Laws of Carbonite, Inc. (Filed as the same numbered exhibit to Amendment No. 2 to Registrant’s Registration Statement on Form S-1 filed with the Securities and Exchange Commission on July 13, 2011, and incorporated herein by reference.) |
| 4.1 | Form of Common Stock Certificate. (Filed as the same numbered exhibit to Amendment No. 3 to Registrant’s Registration Statement on Form S-1/A filed with the Securities and Exchange Commission on July 25, 2011, and incorporated herein by reference) |
| 4.2 | Indenture (including form of Note), dated as of April 4, 2017, by and between Carbonite, Inc. and U.S. Bank National Association, as trustee. (Filed as Exhibit 4.1 to Form 8-K filed with the Securities and Exchange Commission on April 4, 2017 and incorporated herein by reference.) |
| 10.1# | Amended and Restated 2005 Stock Incentive Plan and Form of Incentive Stock Option Agreement, Non-statutory Stock Option Agreement, and Stock Restriction Agreement under the Amended and Restated 2005 Stock Incentive Plan. (Filed as the same numbered exhibit to Amendment No. 2 to Registrant’s Registration Statement on Form S-1/A filed with the Securities and Exchange Commission on July 13, 2011, and incorporated herein by reference.) |
| 10.2# | 2011 Equity Award Plan, as amended. (Filed as Exhibit 10.1 to Form 10-Q filed with the Securities and Exchange Commission on August 3, 2018 and incorporated herein by reference) |
| 10.3# | Form of Indemnification Agreement by and between Carbonite, Inc. and each of its directors and executive officers. (Filed as the same numbered exhibit to Amendment No. 4 to Registrant’s Registration Statement on Form S-1 filed with the Securities and Exchange Commission on May 12, 2011, and incorporated herein by reference.) |
| 10.4 | Commercial Lease with Lewiston Properties, LLC, dated as of May 13, 2011. (Filed as Exhibit 10.13 to Amendment No. 1 to Registrant’s Registration Statement on Form S-1/A filed with the Securities and Exchange Commission on June 15, 2011, and incorporated herein by reference.) |
| 10.5 | Turn Key Datacenter Lease with GIP Wakefield, LLC, dated as of June 3, 2011. (Filed as Exhibit 10.14 to Amendment No. 1 to Registrant’s Registration Statement on Form S-1/A filed with the Securities and Exchange Commission on June 15, 2011, and incorporated herein by reference.) |
| 10.6 | Turn Key Datacenter Lease with Digital Phoenix Van Buren, LLC, dated as of November 29, 2011. (Filed as Exhibit 10.17 to Registrant’s Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 7, 2012, and incorporated herein by reference.) |
| 10.7 | First Amendment to the Datacenter Lease with GIP Wakefield, LLC, dated as of September 15, 2011. (Filed as Exhibit 10.1 to Registrant’s Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on May 3, 2012, and incorporated herein by reference.) |
| 10.8 | Second Amendment to the Datacenter Lease with GIP Wakefield, LLC, dated as of March 31, 2012. (Filed as Exhibit 10.2 to Registrant’s Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on May 3, 2012, and incorporated herein by reference.) |
| 10.9 | Third Amendment to the Datacenter Lease with GIP Wakefield LLC, dated as of June 11, 2012. (Filed as Exhibit 10.24 to Registrant’s Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 6, 2013, and incorporated herein by reference.) |
| 10.10# | Offer Letter with Anthony Folger, dated as of November 21, 2012. (Filed as Exhibit 10.1 to Registrant’s Current Report on Form 8-K filed with the Securities and Exchange Commission on January 2, 2013, and incorporated herein by reference.) |

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| 10.11* | Fourth Amendment to the Datacenter Lease with GIP Wakefield, LLC, dated as of February 14, 2013. (Filed as Exhibit 10.19 to Registrant's Annual Report on Form 10-K with the Securities and Exchange Commission on March 5, 2014, and incorporated herein by reference.) |
| 10.12* | Turnkey Datacenter Lease with Digital 2121 South Price, LLC, dated as of December 31, 2013. (Filed as Exhibit 10.24 to Registrant's Annual Report on Form 10-K with the Securities and Exchange Commission on March 5, 2014, and incorporated herein by reference.) |
| 10.13* | Fifth Amendment to the Datacenter Lease with GIP Wakefield, LLC, dated as of February 6, 2014. (Filed as Exhibit 10.25 to Registrant's Annual Report on Form 10-K with the Securities and Exchange Commission on March 5, 2014, and incorporated herein by reference.) |

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| 10.14 | Indenture of Lease by and between Abbey Lafayette Operating LLC and Carbonite, Inc. dated as of May 5, 2014. (Filed as Exhibit 10.1 to Registrant's Quarterly Report on Form 10-Q with the Securities and Exchange Commission on May 6, 2014, and incorporated herein by reference.) |
| 10.15# | Form of Stock Restriction Agreement under the 2011 Equity Award Plan. (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on June 4, 2014, and incorporated herein by reference.) |
| 10.16# | Amended and Restated Offer Letter with Danielle Sheer, dated as of August 1, 2014. (Filed as Exhibit 10.1 to Registrant's Quarterly Report on Form 10-Q with the Securities and Exchange Commission on August 5, 2014, and incorporated herein by reference.) |
| 10.17# | Promotion Letter Agreement with Cassandra Hudson, dated as of October 28, 2014. (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on November 3, 2014, and incorporated herein by reference.) |
| 10.18* | Sixth Amendment to the Datacenter Lease with GIP Wakefield, LLC, dated as of September 30, 2014. (Filed as Exhibit 10.1 to Registrant's Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 6, 2014, and incorporated herein by reference.) |
| 10.19# | Executive Employment Agreement with Mohamad Ali, dated as of December 3, 2014. (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on December 4, 2014). |
| 10.20# | Amendment to Executive Employment Agreement with Mohamad Ali, dated as of January 8, 2015. (Filed as Exhibit 99.2 to Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on January 9, 2015, and incorporated herein by reference.) |
| 10.21 | Seventh Amendment to the Datacenter Lease with GIP Wakefield, LLC, dated as of September 30, 2015. (Filed as Exhibit 10.1 to Registrant’s Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 9, 2015, and incorporated herein by reference.) |
| 10.22# | Offer Letter with Paul Mellinger, dated as of December 15, 2015. (Filed as Exhibit 10.1 to Registrant’s Current Report on Form 8-K filed with the Securities and Exchange Commission on December 16, 2015, and incorporated herein by reference.) |
| 10.23# | Offer Letter with Norman Guadagno, dated as of January 6, 2016. (Filed as Exhibit 10.1 to Registrant’s Current Report on Form 8-K filed with the Securities and Exchange Commission on January 6, 2016, and incorporated herein by reference.) |
| 10.24# | Amended and Restated Carbonite, Inc. Executive Severance Plan, dated as of May 1, 2018. (Filed as Exhibit 10.2 to Form 10-Q filed with the Securities and Exchange Commission on May 10, 2018 and incorporated herein by reference). |
| 10.25 | Performance-Based Restricted Stock Unit Award Agreement under the 2011 Equity Award Plan. (Filed as Exhibit 10.35 to Registrant’s Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 8, 2016, and incorporated herein by reference.) |
| 10.26 | First Amendment to Turnkey Datacenter Lease with Digital Phoenix Van Buren, LLC, dated as of February 3, 2016. (Filed as Exhibit 10.36 to Registrant’s Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 8, 2016, and incorporated herein by reference.) |
| 10.27* | Eighth Amendment to Turn Key Datacenter Lease with GIP Wakefield, LLC, dated as of September 30, 2016. (Filed as Exhibit 10.1 to Registrant’s Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 9, 2016, and incorporated herein by reference.) |
| 10.28* | Deed of Turn Key Datacenter Lease with Digital Loudoun Parkway Center North, LLC, dated as of September 30, 2016. (Filed as Exhibit 10.2 to Registrant’s Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 9, 2016, and incorporated herein by reference.) |
| 10.29* | Carbonite, Inc. 2017 Employee Stock Purchase Plan (Filed as Appendix B to the Company’s definitive proxy statement filed with the Securities and Exchange Commission on March 27, 2017 and incorporated herein by reference.) |
| 10.30 | |

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| | Credit Agreement, dated as of March 19, 2018 by and between Carbonite, Inc., Silicon Valley Bank, Citizens Bank, N.A., HSBC Bank USA, N.A., Barclays Bank PLC and Wells Fargo Bank, National Association. (Filed as Exhibit 10.1 to Form 8-K filed with the Securities and Exchange Commission on March 19, 2018 and incorporated herein by reference). |
| 10.31# | Senior Executive Severance Plan, dated as of February 2, 2016, as amended. (Filed as Exhibit 10.2 to Form 10-Q filed with the Securities and Exchange Commission on August 3, 2018 and incorporated herein by reference). |
| 10.32# | Employee Severance Plan, as amended. (Filed as Exhibit 10.3 to Form 10-Q filed with the Securities and Exchange Commission on August 3, 2018 and incorporated herein by reference). |

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| Exhibit No. | Description |
|---|---|
| 10.33# | Form of Restricted Stock Unit Agreement under the 2011 Equity Award Plan. (Filed as Exhibit 10.4 to Form 10-Q filed with the Securities and Exchange Commission on August 3, 2018 and incorporated herein by reference). |
| 10.34# | Form of Performance-Based Restricted Stock Unit Award Agreement. (Filed as Exhibit 10.5 to Form 10-Q filed with the Securities and Exchange Commission on August 3, 2018 and incorporated herein by reference). |
| 10.35# | R. Beeler Offer Letter. (Filed as Exhibit 10.1 to Form 10-Q filed with the Securities and Exchange Commission on November 5, 2018 and incorporated herein by reference). |
| 10.36# | Offer Letter Agreement with Linda Connly. (Filed as Exhibit 10.1 to Form 8-K filed with the Securities and Exchange Commission on February 7, 2019 and incorporated herein by reference). |
| 10.37# | Second Amendment to Employment Agreement with Mohamad Ali, dated February 6, 2019. (Filed as Exhibit 10.2 to Form 8-K filed with the Securities and Exchange Commission on February 7, 2019 and incorporated herein by reference). |
| 21.1 | List of subsidiaries. |
| 23.1 | Consent of Deloitte & Touche LLP, independent registered public accounting firm. |
| 23.2 | Consent of Ernst & Young LLP, independent registered public accounting firm. |
| 24.1 | Power of Attorney. |
| 31.1 | Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certifications of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certifications of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.INS | XBRL Instance Document. |
| 101.SCH | XBRL Taxonomy Extension Schema Document. |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document. |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document. |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document. |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document. |

# Indicates a management contract or compensatory plan.
* Portions of this exhibit have been omitted pursuant to the Commission's grant of confidential treatment.