Cornerstone OnDemand Inc
Form 10-Q
May 08, 2018

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

Form 10-Q
(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number 001-35098

Cornerstone OnDemand, Inc.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware | 13-4068197 |
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |

1601 Cloverfield Blvd.
Suite 620 South
Santa Monica, CA 90404
(Address of principal executive offices, including zip code)
Registrant's telephone number, including area code:
(310) 752-0200
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. Yes ¨ No ¨
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No ý
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date

| Class | Outstanding as of May 4, 2018 |
| --- | --- |
| Common Stock | 57,693,211 |

CORNERSTONE ONDEMAND, INC.
QUARTERLY REPORT ON FORM 10-Q
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PART I. FINANCIAL INFORMATION

ITEM 1. Condensed Consolidated Financial Statements

CORNERSTONE ONDEMAND, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except par values)
(unaudited)

| | March 31, 2018 * | December 31, 2017 |
|---|---|---|
| Assets | | |
| Cash and cash equivalents | $413,345 | $ 393,576 |
| Short-term investments | 204,174 | 169,551 |
| Accounts receivable, net | 113,956 | 154,428 |
| Deferred commissions, current portion | 22,830 | 42,806 |
| Prepaid expenses and other current assets | 30,885 | 21,754 |
| Total current assets | 785,190 | 782,115 |
| Capitalized software development costs, net | 39,387 | 37,431 |
| Property and equipment, net | 24,582 | 20,817 |
| Deferred commissions, net of current portion | 34,155 | — |
| Long-term investments | 21,712 | 96,949 |
| Goodwill | 25,894 | 25,894 |
| Other assets, net | 3,813 | 3,984 |
| Total Assets | $934,733 | $ 967,190 |
| Liabilities and Stockholders' Equity | | |
| Liabilities: | | |
| Accounts payable | $10,095 | $ 17,637 |
| Accrued expenses | 48,256 | 57,528 |
| Deferred revenue, current portion | 287,875 | 311,997 |
| Convertible notes, net | 250,497 | 248,025 |
| Other liabilities | 5,570 | 9,051 |
| Total current liabilities | 602,293 | 644,238 |
| Convertible notes, net | 286,256 | 285,168 |
| Other liabilities, non-current | 1,408 | 1,498 |
| Deferred revenue, net of current portion | 12,415 | 14,166 |
| Total liabilities | 902,372 | 945,070 |
| Commitments and contingencies (Note 10) | | |
| Stockholders' Equity: | | |
| Common stock, $0.0001 par value; 1,000,000 shares authorized, 57,525 and 57,512 shares issued and outstanding at March 31, 2018 and December 31, 2017, respectively | 6 | 6 |
| Additional paid-in capital | 546,808 | 536,951 |
| Accumulated deficit | (512,335) | (515,054) |
| Accumulated other comprehensive (loss) income | (2,118) | 217 |
| Total stockholders' equity | 32,361 | 22,120 |
| Total Liabilities and Stockholders' Equity | $934,733 | $ 967,190 |

*See Note 1 for summary of adjustments.

See accompanying notes to unaudited condensed consolidated financial statements.

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CORNERSTONE ONDEMAND, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 * | 2017 |
| Revenue | $133,113 | $111,582 |
| Cost of revenue | 37,020 | 33,949 |
| Gross profit | 96,093 | 77,633 |
| Operating expenses: | | |
| Sales and marketing | 59,245 | 56,894 |
| Research and development | 15,984 | 13,411 |
| General and administrative | 21,985 | 20,476 |
| Restructuring | 7,725 | — |
| Total operating expenses | 104,939 | 90,781 |
| Loss from operations | (8,846) | (13,148) |
| Other income (expense): | | |
| Interest income | 1,819 | 613 |
| Interest expense | (8,700) | (3,302) |
| Other, net | 44 | 197 |
| Other income (expense), net | (6,837) | (2,492) |
| Loss before income tax provision | (15,683) | (15,640) |
| Income tax provision | (533) | (571) |
| Net loss | $(16,216) | $(16,211) |
| Net loss per share, basic and diluted | $(0.28) | $(0.29) |
| Weighted average common shares outstanding, basic and diluted | 57,425 | 56,642 |

*See Note 1 for summary of adjustments.

See accompanying notes to unaudited condensed consolidated financial statements.

CORNERSTONE ONDEMAND, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(in thousands)
(unaudited)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 * | 2017 |
| Net loss | $(16,216) | $(16,211) |
| Other comprehensive loss, net of tax: | | |
| Foreign currency translation adjustment | (2,111) | (174) |
| Net change in unrealized losses on investments | (225) | (87) |
| Other comprehensive loss, net of tax | (2,336) | (261) |
| Total comprehensive loss | $(18,552) | $(16,472) |

*See Note 1 for summary of adjustments.

See accompanying notes to unaudited condensed consolidated financial statements.

CORNERSTONE ONDEMAND, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 * | 2017 |
| Cash flows from operating activities: | | |
| Net loss | $(16,216) | $(16,211) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation and amortization | 7,831 | 9,328 |
| Accretion of debt discount and amortization of debt issuance costs | 3,426 | 2,353 |
| Purchased investment premium, net of amortization | (81) | 155 |
| Net foreign currency gain | (356) | (530) |
| Stock-based compensation expense | 19,479 | 15,849 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 41,888 | 38,257 |
| Deferred commissions | (528) | 1,718 |
| Prepaid expenses and other assets | (8,841) | (7,433) |
| Accounts payable | (7,605) | (14,485) |
| Accrued expenses | (15,059) | (13,776) |
| Deferred revenue | (23,751) | (22,637) |
| Other liabilities | (4,767) | 177 |
| Net cash used in operating activities | (4,580) | (7,235) |
| Cash flows from investing activities: | | |
| Purchases of investments | — | (77,281) |
| Maturities of investments | 40,677 | 65,487 |
| Capital expenditures | (2,559) | (2,698) |
| Capitalized software costs | (6,039) | (5,756) |
| Net cash provided by (used in) investing activities | 32,079 | (20,248) |
| Cash flows from financing activities: | | |
| Payments of debt issuance costs | (152) | — |
| Proceeds from employee stock plans | 6,765 | 3,473 |
| Repurchases of common stock | (14,700) | — |
| Net cash (used in) provided by financing activities | (8,087) | 3,473 |
| Effect of exchange rate changes on cash and cash equivalents | 357 | 570 |
| Net increase (decrease) in cash and cash equivalents | 19,769 | (23,440) |
| Cash and cash equivalents at beginning of period | 393,576 | 83,300 |
| Cash and cash equivalents at end of period | $413,345 | $59,860 |
| Supplemental cash flow information: | | |
| Cash paid for interest | $3,000 | $1,898 |
| Cash paid for income taxes | 452 | 648 |
| Proceeds from employee stock plans received in advance of stock issuance | 1,616 | 1,393 |
| Non-cash investing and financing activities: | | |
| Capitalized assets financed by accounts payable and accrued expenses | $5,201 | $623 |
| Capitalized stock-based compensation | 1,253 | 1,135 |
| Unsettled share repurchase in other liabilities | 1,325 | — |

*See Note 1 for additional information.

See accompanying notes to unaudited condensed consolidated financial statements.

CORNERSTONE ONDEMAND, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Company Overview

Cornerstone OnDemand, Inc. ("Cornerstone" or the "Company") was incorporated on May 24, 1999 in the state of Delaware and began its principal operations in November 1999.

The Company is a leading global provider of learning and human capital management software, delivered as Software-as-a-Service ("SaaS"). The Company helps organizations around the globe recruit, train and manage their employees. It is one of the world's largest cloud computing companies. The Company's human capital management platform combines the world's leading unified talent management solutions with state-of-the-art analytics and HR administration solutions to enable organizations to manage the entire employee lifecycle. Its focus on continuous learning and development helps organizations to empower employees to realize their potential and drive success. The Company works with clients across all geographies, verticals and market segments. Its Recruiting, Learning, Performance and HR Administration suites help with sourcing, recruiting and onboarding new hires; managing training and development requirements; nurturing knowledge sharing and collaboration among employees; goal setting reviews, competency management and continuous feedback; linking compensation to performance; identifying development plans based on performance gaps; streamlining employee data management, self-service and compliance reporting; and then utilizing state-of-the-art analytics capabilities to make smarter, more-informed decisions using data from across the platform for talent mobility, engagement and development so that HR and leadership can focus on strategic initiatives to help their organization succeed.

The Company's management has determined that the Company operates in one segment as it only reports financial information on an aggregate and consolidated basis to the Company's chief executive officer, who is the Company's chief operating decision maker.

### Office Locations

The Company is headquartered in Santa Monica, California and has offices in Amsterdam, Netherlands; Auckland, New Zealand; Bangalore, India; Düsseldorf, Germany; Hong Kong; London, United Kingdom; Madrid, Spain; Mumbai, India; Munich, Germany; Paris, France; São Paulo, Brazil; Stockholm, Sweden; Sunnyvale, United States; Sydney, Australia; Tel Aviv, Israel; and Tokyo, Japan.

### Basis of Presentation

The accompanying unaudited condensed consolidated financial statements are presented in accordance with (i) accounting standards generally accepted in the United States of America ("GAAP") for interim financial information and (ii) the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, such financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, the financial statements include all adjustments (consisting of normal recurring adjustments) necessary for the fair presentation of the interim periods presented. Results for the three months ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018, for any other interim period or for any other future year.

The condensed consolidated balance sheet at December 31, 2017 has been derived from the audited financial statements at that date, but does not include all of the disclosures required by GAAP.

The Company's significant accounting policies are described in "Note 2. Summary of Significant Accounting Policies" in the Company's Annual Report on Form 10-K for the year ended December 31, 2017. The Company follows the same accounting policies for interim reporting. The financial information included in this Quarterly Report on Form 10-Q should be read in conjunction with the Company's consolidated financial statements and related notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

Effective January 1, 2018, the Company adopted the requirements of Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers, as discussed further in Note 1. All amounts and disclosures set forth in this Quarterly Report on Form 10-Q have been updated to comply with this new standard with results for reporting periods beginning after January 1, 2018 presented under ASU No. 2014-09, while prior period amounts are

not adjusted and continue to be reported under the accounting standards in effect for the prior period.

Recently Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued ASU No. 2014-09, Revenue from Contracts with Customers (“Topic 606”). Topic 606 supersedes the revenue recognition requirement in Accounting Standards Codification (“ASC”) Topic 605, Revenue Recognition (“Topic 605”), and requires the recognition of revenue to depict the transfer of promised goods or services to customers in an amount that reflects the expected consideration entitled in exchange for those goods or services. Topic 606 also includes Subtopic 340-40, Other Assets and Deferred Costs - Contracts with Customers, which requires the deferral of incremental costs of obtaining a contract with a customer.

The Company adopted the requirements of Topic 606 utilizing the modified retrospective method of transition to contracts as of January 1, 2018. The accumulated deficit balance was reduced, thus stockholders' equity was increased by $18.9 million as of January 1, 2018 due to the cumulative impact of adopting Topic 606. The impact was primarily related to:

- $15.5 million increase in deferred commissions. Such costs are considered to be costs to acquire a contract under Topic 606, and primarily relate to the execution of software subscription contracts. In addition, upon adoption, these incremental commission costs to obtain a contract are now amortized over a period of benefit, which is generally six years.
- $2.7 million of additional liability offsets the impact to retained earnings from the increase of the deferred commission above. The liability is to accrue commission costs earned but not yet paid.
- $6.1 million reduction in deferred revenue related to additional contract value being allocated to professional services delivered prior to adoption. Previously such amounts were not recognized based on contractual payment limitations. Upon adoption, revenue for professional services is based on the relative standalone selling price without any such limitation.

The adoption had no impact to net cash provided by or used in operating. investing or financing activities in the Company’s Condensed Consolidated Statements of Cash Flows.

In May 2017, the FASB issued a new ASU, which amends the scope of modification accounting for share-based payment arrangements. It provides guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting under ASC 718. The Company implemented this requirement as of the beginning of the first quarter of 2018. The adoption did not have a material impact on its financial statements.

In August 2016, the FASB issued a new ASU to clarify how companies present and classify certain cash receipts and cash payments in the statement of cash flows. The Company implemented this requirement as of the beginning of the first quarter of 2018. The adoption did not have a material impact on its financial statements.

In January 2016, the FASB issued a new ASU that provides guidance for the recognition, measurement, presentation and disclosure of financial assets and liabilities. The Company implemented this requirement as of the beginning of the first quarter of 2018. The adoption did not have a material impact on its financial statements.

Summary of Significant Accounting Policies

Except for changes to the Company's revenue recognition policy and the accounting for commission payments, there have been no changes to the Company’s significant accounting policies described in the Annual Report on Form 10-K for the year ended December 31, 2017, filed with the SEC on February 27, 2018. See below for additional accounting policy and transition disclosures.

Revenue Recognition

Effective January 1, 2018, the Company adopted the guidance under Topic 606.

The Company derives its revenue from the following sources:

Subscriptions to the Company’s products and other offerings on a recurring basis

Clients pay subscription fees for access to the Company’s enterprise human capital management platform, other products and support on a recurring basis. Fees are based on a number of factors, including the number of products purchased, which may include e-learning content, and the number of users having access to a product. The Company generally recognizes revenue from subscriptions ratably over the term of the agreements beginning on the date the subscription service is made available to the client. Subscription agreements are typically three years, billed annually in advance, and non-cancelable.

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Professional services and other

The Company offers its clients and implementation partners assistance in implementing its products and optimizing their use. Professional services include application configuration, system integration, business process re-engineering, change management and training services. Services are generally billed up-front on a fixed fee basis and to a lesser degree on a time-and-material basis. These services are generally purchased as part of a subscription arrangement and are typically performed within the first several months of the arrangement. Clients may also purchase professional services at any other time. The Company generally recognizes revenue from fixed fee professional services contracts as services are performed based on the proportion performed to date relative to the total expected services to be performed. Revenue associated with time-and-material contracts are recorded as such time-and-materials are incurred.

The Company recognizes revenue from contracts with customers based on the following five steps:

1) Identification of the contract, or contracts, with a customer
2) Identification of all performance obligations in the contract
3) Determination of the transaction price
4) Allocation of the transaction price to the performance obligations in the contract
5) Recognition of revenue as we satisfy a performance obligation

The Company identifies enforceable contracts with a customer when the agreement is signed. The Company accounts for individual performance obligations separately if they are distinct. The transaction price is generally based on fixed fees stated in the contract. The Company excludes from the transaction price any amounts relating to taxes from product sales which are collected from customers and remitted to governmental authorities. If the contract contains a single performance obligation, the entire transaction price is allocated to the single performance obligation. Contracts that contain multiple performance obligations require an allocation of the transaction price to each performance obligation based on a relative standalone selling price basis. The Company is not able to directly observe a standalone selling price for its performance obligations, as the performance obligations are sold separately and within a sufficiently narrow price range only infrequently, and because management has determined that there are no third-party offerings reasonably comparable to the Company's products. Accordingly, total contract values are allocated to subscriptions to the products and professional services based on management's best estimate of the selling price ("BESP"). The determination of BESP requires the Company to make significant estimates and judgments. The Company considers numerous factors, including the nature and complexity of the performance obligations themselves; the geography, market conditions and competitive landscape for the sale; internal costs; and pricing and discounting practices. The Company updates its estimates of BESP on an ongoing basis through internal periodic reviews and as events or circumstances may require. Revenue is recognized at the time the related performance obligation is satisfied by transferring a promised service to a customer. The Company satisfies performance obligations over time.

In a limited number of cases, the client's intended use of a product requires contractually specified enhancements to its underlying features and functionality. In some of these cases, revenue is recognized as a combined single performance obligation on a straight-line basis from the point at which access to the enhanced product(s) have been provided, through the remaining term of the agreement. In other cases where the enhancement is not contractually specified by the customer for its initial use and revenue is recognized separately for the enhancement and the product as a second distinct performance obligation. In such cases where a second performance obligation exists, the enhancement revenue is recognized based on a BESP allocation on a straight-line basis once access to the enhancement has been provided, through the remaining term of the agreement.

For arrangements in which the Company resells third-party e-learning training content to clients, revenue is recognized in accordance with accounting guidance as to when to report gross revenue as a principal or report net revenue as an agent. The Company typically recognizes third-party content revenue at the gross amount invoiced to clients as (i) the Company is primarily responsible for hosting the content on our platform for the term of the agreement, (ii) the Company controls the content before access is provided to the customer, and (iii) the Company typically has discretion to establish the price charged.

Deferred Revenue

The Company records amounts that have been invoiced to its clients in accounts receivable and in either deferred revenue or revenue depending on whether the revenue recognition criteria described above have been met. Deferred revenue that will be recognized during the succeeding twelve-month period from the respective balance sheet date is recorded as current deferred revenue and the remaining portion is recorded as noncurrent. The decrease in the deferred revenue balance for the three months ended March 31, 2018 is primarily driven by $119.4 million of revenues recognized that were included in the deferred revenue balances as of January 1, 2018 offset by invoices billed in advance of satisfying performance obligations in accordance with contract payment terms.

Transaction Price Allocated to Remaining Performance Obligations

As of March 31, 2018, approximately $790.0 million of revenue is expected to be recognized from remaining performance obligations. This is substantially comprised of subscription revenue, with less than 10% attributed to professional services and other revenue. The Company expects to recognize revenue on approximately two thirds of these remaining performance obligations over the next 18 months, with the balance recognized thereafter.

The estimated revenues from the remaining performance obligations do not include uncommitted contract amounts such as (i) amounts which are cancelable by the client without any significant penalty, (ii) future billings for time and material contracts, and (iii) amounts associated with optional renewal periods.

Commission Payments

The Company defers commissions paid to its sales force and related payroll taxes as these amounts are incremental costs of obtaining a contract with a customer and are recoverable from future revenue due to the non-cancelable client agreements that gave rise to the commissions. Commissions for initial contracts are deferred on the balance sheet and amortized on a straight-line basis over a period of benefit that has been determined to be six years. The Company took into consideration technology and other factors in estimating the benefit period. Sales commissions for renewal contracts are deferred and amortized on a straight-line basis over the related contract renewal period. Amortization expense is included in sales and marketing expenses in the accompanying condensed consolidated statements of operations.

Impact of New Standard on Financial Statement Line Items

The following tables summarize the effect of the adoption of Topic 606 on the Company’s select line items, included in the unaudited consolidated condensed financial statements as of and for the quarter ended March 31, 2018, as if the previous accounting was in effect (in thousands).

| Condensed Consolidated Balance Sheet | March 31, 2018 | | |
|---|---|---|---|
| | As Reported (ASC 606) | Impacts of Adoption | Without Adoption (ASC 605) |
| Assets | | | |
| Deferred commissions, current portion | $22,830 | $18,207 | $41,037 |
| Deferred commissions, non-current | 34,155 | (34,155) | — |
| Liabilities | | | |
| Accrued expenses | 48,256 | (2,625) | 45,631 |
| Deferred revenue, current portion | 287,875 | 6,501 | 294,376 |
| Stockholders' Equity | | | |
| Accumulated deficit | (512,335) | (19,824) | (532,159) |

| Condensed Consolidated Statement of Operations | March 31, 2018 | | |
|---|---|---|---|
| | As Reported (ASC 606) | Impacts of Adoption | Without Adoption (ASC 605) |
| Revenue | $133,113 | $ (441) | $132,672 |
| Operating expenses: | | | |
| Sales and marketing | 59,245 | 300 | 59,545 |
| Net loss | (16,216) | (741) | (16,957) |
| Net loss per share, basic and diluted | (0.28) | | (0.30) |
| Weighted average common shares outstanding, basic and diluted | 57,425 | | 57,425 |

The adoption of Topic 606 had no impact to net cash from or used in operating, investing or financing activities in the Company's unaudited condensed statement of cash flows from for the quarter ended March 31, 2018.

Recent Accounting Pronouncements

In February 2016, the FASB issued a new ASU, which amends a number of aspects of lease accounting, including requiring lessees to recognize operating leases with a term greater than one year on their balance sheet as a right-of-use asset and corresponding lease liability, measured at the present value of the lease payments. This guidance is effective for the Company's interim and annual reporting periods beginning January 1, 2019. Upon adoption, the Company expects additional lease liability to be recognized on the consolidated balance sheets.

2. NET LOSS PER SHARE

The following table presents the Company's basic and diluted net loss per share (in thousands, except per share amounts):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Net loss | $(16,216) | $(16,211) |
| Weighted-average shares of common stock outstanding | 57,425 | 56,642 |
| Net loss per share – basic and diluted | $(0.28) | $(0.29) |

At March 31, 2018 and 2017, the following potential shares were excluded from the computation of diluted net loss per share because their effect would have been anti-dilutive (in thousands):

| | March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Options to purchase common stock, restricted stock units and performance-based restricted stock units | 11,629 | 11,324 |
| Shares issuable pursuant to employee stock purchase plan | 114 | 89 |
| Convertible notes | 11,825 | 4,682 |
| Common stock warrants | 4,682 | 4,682 |
| Total shares excluded from net loss per share | 28,250 | 20,777 |

Under the treasury stock method, the convertible notes and common stock warrants will have a dilutive impact on net earnings per share when the average stock price for the period exceeds the respective conversion prices and the Company has net income. The Company also entered into note hedge transactions ("Note Hedges") in connection with the convertible notes with respect to its common stock to minimize the impact of potential economic dilution upon conversion of the convertible notes. The Note Hedges were outstanding as of March 31, 2018. Since the beneficial impact of the Note Hedges is anti-dilutive, they are excluded from the calculation of diluted net income (loss) per share. See Note 5 of the Notes to Condensed Consolidated Financial Statements.

3. INVESTMENTS

Investments in Marketable Securities

The Company's investments in available-for-sale marketable securities are made pursuant to its investment policy, which has established guidelines relative to the diversification of the Company's investments and their maturities, with the principal objective of capital preservation and maintaining liquidity that is sufficient to meet cash flow requirements.

The following is a summary of investments in marketable securities, including those that meet the definition of a cash equivalent, as of March 31, 2018 (in thousands):

| | March 31, 2018 | | | | | |
|---|---|---|---|---|---|---|
| | Amortized Cost Basis | Unrealized Gains | Unrealized Losses | Fair Value | Cash Equivalent | Investments |
| Money market funds | $372,445 | $ — | $ — | $372,445 | $ 372,445 | $ — |
| Certificate of deposit | 10,000 | — | — | 10,000 | 10,000 | — |
| Corporate bonds | 65,298 | — | (350) | 64,948 | — | 64,948 |
| U.S. treasury securities | 158,491 | — | (525) | 157,966 | — | 157,966 |
| | $606,234 | $ — | $ (875) | $605,359 | $ 382,445 | $ 222,914 |

The following is a summary of investments in marketable securities, including those that meet the definition of a cash equivalent, as of December 31, 2017 (in thousands):

| | December 31, 2017 | | | | | |
|---|---|---|---|---|---|---|
| | Amortized Cost Basis | Unrealized Gains | Unrealized Losses | Fair Value | Cash Equivalent | Investments |
| Money market funds | $358,859 | $ — | $ — | $358,859 | $ 358,859 | $ — |
| Certificate of deposit | 10,000 | — | — | 10,000 | 10,000 | — |
| Corporate bonds | 74,868 | — | (220) | 74,648 | — | 74,648 |
| U.S. treasury securities | 189,310 | — | (430) | 188,880 | — | 188,880 |
| | $633,037 | $ — | $ (650) | $632,387 | $ 368,859 | $ 263,528 |

As of March 31, 2018, the Company's investment in corporate bonds, agency bonds and U.S. treasury securities had a weighted-average maturity date of approximately seven months. Unrealized gains and losses on investments were not significant and the Company does not believe the unrealized losses represent other-than-temporary impairments as of March 31, 2018 and December 31, 2017. No marketable securities held have been in a continuous unrealized loss position for more than 12 months as of March 31, 2018 and December 31, 2017.

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Strategic Investments

As of March 31, 2018, the Company had aggregate strategic investments of $3.0 million. The Company accounted for each of these investments using the cost method of accounting, as the Company does not have significant influence or a controlling financial interest over these entities.

These investments are subject to periodic impairment reviews and are considered to be impaired when a decline in fair value is judged to be other-than-temporary. During the three months ended March 31, 2018, the Company did not recognize any impairment losses. During the three months ended March 31, 2017 , the Company recognized $0.6 million of impairment losses.

4. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value represents the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. Observable inputs are based on market data obtained from independent sources. The fair value hierarchy is based on the following three levels of inputs, of which the first two are considered observable and the last one is considered unobservable:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 – Unobservable inputs.

Assets and liabilities measured at fair value on a recurring basis included the following as of March 31, 2018 and December 31, 2017 (in thousands):

| | March 31, 2018 | | | | December 31, 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Fair Value | Level 1 | Level 2 | Level 3 | Fair Value | Level 1 | Level 2 | Level 3 |
| Cash equivalents | $382,445 | $372,445 | $10,000 | $ — | $368,859 | $358,859 | $10,000 | $ — |
| Corporate bonds | 64,948 | — | 64,948 | — | 74,648 | — | 74,648 | — |
| U.S. treasury securities | 157,966 | — | 157,966 | — | 188,880 | — | 188,880 | — |
| | $605,359 | $372,445 | $232,914 | $ — | $632,387 | $358,859 | $273,528 | $ — |

At March 31, 2018 and December 31, 2017, cash equivalents of $372.4 million and $358.9 million, respectively, consisted of money market funds with original maturity dates of three months or less backed by U.S. Treasury bills.

At March 31, 2018 and December 31, 2017, cash equivalents of $10.0 million and $10.0 million, respectively, consisted of certificate of deposits with original maturity dates of three months or less.

As of March 31, 2018, corporate bonds, agency bonds, U.S. treasury securities and commercial paper were classified within Level 2 of the fair value hierarchy. The bonds were valued using information obtained from pricing services, which obtained quoted market prices from a variety of industry data providers, security master files from large financial institutions, and other third-party sources. The Company performed supplemental analysis to validate information obtained from its pricing services. As of March 31, 2018, no adjustments were made to such pricing information.

Convertible Notes

The Company’s convertible notes, including the 2018 Notes and the 2021 Notes described below, are shown in the accompanying Condensed Consolidated Balance Sheets at their original issuance value, net of unamortized discount and debt issuance costs, and are not remeasured to fair value each period. The approximate fair value of the Company’s convertible notes as of March 31, 2018 was $552.9 million. The fair value of the 2018 Notes was estimated on the basis of quoted market prices, which, due to limited trading activity, are considered Level 2 in the fair value hierarchy. The fair value of the 2021 Notes was estimated on the basis of quoted market prices, which, due to the lack of trading activity, are considered Level 2 in the fair value hierarchy.

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5. DEBT

2018 Convertible Notes

In 2013, the Company issued convertible notes (the "2018 Notes") raising gross proceeds of $253.0 million.

The 2018 Notes are governed by an Indenture, dated June 17, 2013, between the Company and U.S. Bank National Association, as trustee (the "2013 Indenture"). The 2018 Notes mature on July 1, 2018, unless earlier repurchased or converted, and bear interest at a rate of 1.50% per year payable semi-annually in arrears on January 1 and July 1 of each year, commencing January 1, 2014.

The 2018 Notes are convertible at an initial conversion rate of 18.5046 shares of the Company's common stock per $1,000 principal amount of the 2018 Notes, which represents an initial conversion price of approximately $54.04 per share, subject to adjustment for anti-dilutive issuances, voluntary increases in the conversion rate and make-whole adjustments upon a fundamental change. A fundamental change includes a change in control, delisting of the Company's common stock and a liquidation of the Company. Upon conversion, the Company will deliver cash for the principal amount, and the Company has the right to settle any amounts in excess of the principal in cash or shares.

Prior to April 1, 2018, the 2018 Notes are only convertible upon satisfaction of certain conditions as follows:

- during any calendar quarter after September 30, 2013, if the last reported sale price of common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter is greater than or equal to 130% of the conversion price on each applicable trading day;
- during the five business day period after any five consecutive trading day period in which the trading price per $1,000 principal amount of the 2018 Notes for each trading day of that five consecutive trading day period was less than 98% of the product of the last reported sale price of common stock and the conversion rate on each such trading day; or
- upon the occurrence of specified corporate events as defined in the 2013 Indenture.

Holders of the 2018 Notes may convert their 2018 Notes at any time on or after April 1, 2018, until the close of business on the second scheduled trading day immediately preceding the maturity date. As of the date of this filing, there have not been any elected conversions.

The holders of the 2018 Notes may require the Company to repurchase all or a portion of their 2018 Notes at a cash repurchase price equal to 100% of the principal amount of the 2018 Notes being repurchased, plus accrued and unpaid interest, upon a fundamental change and events of default, including non-payment of interest or principal and other obligations under the 2013 Indenture.

In accounting for the 2018 Notes at issuance, the Company separated the 2018 Notes into debt and equity components pursuant to the accounting standards for convertible debt instruments that may be fully or partially settled in cash upon conversion. The fair value of the debt component was estimated using an interest rate for nonconvertible debt, with terms similar to the 2018 Notes, excluding the conversion feature. The excess of the principal amount of the 2018 Notes over the fair value of the debt component was recorded as a debt discount and a corresponding increase in additional paid-in capital. The debt discount is accreted to interest expense over the term of the 2018 Notes using the interest method. The amount recorded to additional paid-in capital is not to be remeasured as long as it continues to meet the conditions for equity classification. Upon issuance of the $253.0 million of 2018 Notes, the Company recorded $214.3 million to debt and $38.7 million to additional paid-in capital for the debt discount.

The Company incurred transaction costs of approximately $7.3 million related to the issuance of the 2018 Notes. In accounting for these costs, the Company allocated the costs to the debt and equity components in proportion to the allocation of proceeds from the issuance of the 2018 Notes to such components. Transaction costs allocated to the debt component of $6.2 million are deferred and amortized to interest expense over the term of the 2018 Notes. The transaction costs allocated to the equity component of $1.1 million were recorded to additional paid-in capital.

2021 Senior Convertible Notes

In December 2017, the Company issued $300.0 million principal amount of 5.75% senior convertible notes (the "2021 Notes") for a purchase price equal to 98% of the principal amount, raising net proceeds of $294.0 million.

The 2021 Notes are governed by an Indenture, dated December 8, 2017 between the Company and U.S. Bank National Association, as trustee (the "2017 Indenture"). The 2021 Notes mature on July 1, 2021, unless earlier repurchased or converted, and bear interest at a rate of 5.75% per year payable semi-annually in arrears on January 1 and July 1 of each year, commencing January 1, 2018.

The 2021 Notes are convertible at an initial conversion rate of 23.8095 shares of the Company's common stock per $1,000 principal amount of the 2021 Notes, which represents an initial conversion price of $42.00 per share, subject to adjustment for anti-dilutive issuances, voluntary increases in the conversion rate and make-whole adjustments upon a fundamental change. A fundamental change includes a change in control, delisting of the Company's common stock and a liquidation of the Company. Upon conversion, the Company will deliver the applicable number of the Company's common stock and cash in lieu of any fractional shares. Holders of the 2021 Notes may convert their 2021 Notes at any time prior to the close of business on the scheduled trading day immediately preceding the maturity date, subject to a restricted period through December 2018.

The holders of the 2021 Notes may require the Company to repurchase all or a portion of their 2021 Notes at a cash repurchase price equal to 100% of the principal amount of the Notes being repurchased, plus the remaining scheduled interest through and including the maturity date, upon a fundamental change and events of default, including non-payment of interest or principal and other obligations under the 2017 Indenture.

The 2021 Notes were issued at a two percent discount and was accounted for as debt upon issuance. The Company recorded $300.0 million of debt and $6.0 million for the debt discount. The debt discount is accreted to interest expense over the term of the 2021 Notes using the interest method.

The Company incurred debt issuance costs of $9.1 million that were deferred and will be amortized to interest expense over the term of the 2021 Notes.

2018 Notes and 2021 Notes

The net carrying amounts of the liability components of the 2018 and 2021 Notes as of March 31, 2018 and December 31, 2017 consists of the following (in thousands):

| | March 31, 2018 | December 31, 2017 |
|---|---|---|
| Principal amount | $553,000 | $ 553,000 |
| Unamortized debt discount | (7,680) | (10,190) |
| Net carrying amount before unamortized debt issuance costs | 545,320 | 542,810 |
| Unamortized debt issuance costs | (8,567) | (9,617) |
| Net carrying value | $536,753 | $ 533,193 |

The effective interest rate of the liability component is 5.4% and 6.4% for the 2018 Notes and the 2021 Notes, respectively. The interest rate for the 2018 Notes was based on the interest rates of similar liabilities at the time of issuance that did not have associated convertible features.

The following table presents the interest expense recognized related to the 2018 Notes and the 2021 Notes for the three months ended March 31, 2018 and 2017 (in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Contractual interest expense at 1.5% and 5.75% per annum | $5,261 | $949 |
| Amortization of debt issuance costs | 916 | 326 |
| Accretion of debt discount | 2,510 | 2,028 |
| Total | $8,687 | $3,303 |

Net proceeds were approximately $245.7 million and $284.9 million from the 2018 Notes and the 2021 Notes, respectively. The Company used approximately $49.5 million of the net proceeds of the 2018 Notes offering to pay the cost of the Note Hedges described below, which was partially offset by $23.2 million of the proceeds from the Company's sale of the Warrants also described below.

Note Hedges

Concurrent with the 2018 Notes that were issued in 2013, the Company entered into note hedges (the "Note Hedges") with certain bank counterparties, with respect to its common stock. The Company paid $49.5 million for the Note Hedges. The Note Hedges cover approximately 4.7 million shares of the Company's common stock at a strike price of $54.04 per share and are exercisable by the Company upon conversion of the 2018 Notes. The Note Hedges will expire upon the maturity of the 2018 Notes. The Note Hedges are intended to reduce the potential economic dilution upon conversion of the 2018 Notes in the event that the fair value per share of the Company's common stock at the time of exercise is greater than the conversion price of the 2018 Notes.

Warrants

Separately and concurrently with the entry by the Company into the Note Hedges in 2013, the Company entered into warrant transactions, whereby it sold warrants to the same bank counterparties as the Note Hedges to acquire up to 4.7 million shares of the Company's common stock at a strike price of $80.06 per share (the "Warrants"), subject to anti-dilution adjustments. The Company received proceeds of $23.2 million from the sale of the Warrants. The Warrants expire at various dates during 2018 and 2019. If the fair value per share of the Company's common stock exceeds the strike price of the Warrants, the Warrants will reduce diluted earnings per share to the extent that the calculation does not have an anti-dilutive effect.

The amounts paid and received for the Note Hedges and the Warrants have been recorded in additional paid-in capital. The fair value of the Note Hedges and the Warrants are not remeasured through earnings each reporting period.

6. STOCKHOLDERS' EQUITY

Share Repurchase Program

In November 2017, the Company's board of directors authorized a $100.0 million share repurchase program of its common stock. The Company may repurchase its common stock for cash in the open market in accordance with applicable securities laws. The timing and amount of any stock repurchase will depend on share price, corporate and regulatory requirements, economic and market conditions, and other factors. The stock repurchase authorization will expire in November 2019 and shares repurchased will be immediately retired.

The following is a summary of the Company's stock repurchases as of May 4, 2018 (in thousands, except per share information):

| Period | # of Shares Repurchased | Average Price per Share | Total Expenditures |
|---|---|---|---|
| November 8, 2017 - December 31, 2017 | 635 | $ 35.55 | $ 22,599 |
| January 1, 2018 - March 31, 2018 | 423 | $ 37.84 | 16,024 |
| April 1, 2018 - May 4, 2018 | 100 | $ 39.44 | 3,988 |
| Total | 1,158 | $ 36.74 | $ 42,611 |

At March 31, 2018, $61.4 million remained available under the share repurchase program.

7. STOCK-BASED AWARDS

Stock Options

The following table summarizes the Company's stock option activity for the three months ended March 31, 2018 (in thousands, except per share and term information):

| | Shares | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value (1) |
|---|---|---|---|---|
| Outstanding, December 31, 2017 | 5,294 | $ 32.99 | 5.3 | $ 40,122 |
| Granted | — | — | | |
| Exercised | (211) | 24.44 | | |
| Forfeited | (56) | 45.81 | | |
| Outstanding, March 31, 2018 | 5,027 | $ 33.21 | 4.9 | $ 47,595 |

| | Shares | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value (1) |
|---|---|---|---|---|
| Exercisable at March 31, 2018 | 4,786 | $ 33.00 | 4.8 | $ 46,840 |
| Vested and expected to vest at March 31, 2018 | 5,017 | 33.20 | 4.9 | 47,561 |

(1) Based on the Company's closing stock price of $39.11 on March 31, 2018 and $35.33 on December 31, 2017.

Unrecognized compensation expense relating to stock options was $3.2 million at March 31, 2018, which is expected to be recognized over a weighted-average period of 0.9 years.

Restricted Stock Units

The Company granted restricted stock units covering 0.8 million shares of its common stock during the three months ended March 31, 2018. At March 31, 2018, there were 4.2 million shares of the Company's common stock issuable upon the vesting of outstanding restricted stock units. Unrecognized compensation expense related to unissued shares of the Company's common stock subject to unvested restricted stock units was $119.1 million at March 31, 2018, which is expected to be recognized as expense over the weighted-average period of 3.0 years.

Performance-Based Restricted Stock Units

The Compensation Committee designed an annual equity compensation structure to further align the compensation levels of certain executives to the performance of the Company through the issuance of performance-based restricted stock units. The number of shares of the Company's common stock issuable upon the vesting of these performance-based restricted stock unit awards is based upon the Company meeting composite revenue and cash flow growth targets determined at the time of their grants. The total amount of compensation expense recognized is based on the number of shares that the Company determines are probable of vesting. The estimate will be made each reporting period and determined by the Company's actual and projected revenue and cash flow performance and the compensation expense will be recognized over the vesting term of the awards.

The following table summarizes the Company's issuances of awards under the new compensation award structure:

| Grant Date | Performance Measures | Vesting Term | Performance Period | # of Shares at Target | # of Shares at Maximum | Grant Date Fair Value per share |
|---|---|---|---|---|---|---|
| July 2016 | (a) the Company meeting certain revenue and cash flow targets through December 31, 2018 and (b) the recipient continuing to provide services to the Company through the end of June 2019 | Three years | Fiscal years 2016, 2017 and 2018 | 166,600 | 499,800 | $38.67 |
| March 2017 | (a) the Company meeting certain revenue and cash flow targets through December 31, 2019 and (b) the recipient continuing to provide services to the Company through the end of March 2020 | Three years | Fiscal years 2017, 2018 and 2019 | 185,270 | 555,810 | $41.73 |
| February 2018 | (a) the Company meeting certain combined subscription revenue and unlevered cash flow margin targets for the year ending December 31, 2020 and (b) the recipient continuing to provide services to the Company through the end of February 2021 | Three years | Fiscal year 2020 | 121,764 | 304,410 | $40.64 |
| February 2018 | (a) the Company meeting certain combined subscription revenue and unlevered cash flow margin targets for each of the years ending December 31, 2020, December 31, 2021, and December 31, 2022 and (b) the recipient continuing to provide services to the Company through the end of February 2023 | Five years | Fiscal years 2020, 2021 and 2022 (1) | 411,412 | 1,028,530 | $40.64 |

(1) One-third of the total eligible shares shall vest on each of the third, fourth and fifth anniversaries of the grant date. This award is a one-time equity award intended to cover expected grant levels over a three-year period. In exchange, the Compensation Committee does not plan to grant any additional equity awards to recipients of this award until 2021.

The Company recognized compensation expense related to all performance-based awards in the aggregate amount of $0.5 million and $3.1 million for the three months ended March 31, 2018 and 2017, respectively. There was no unrecognized compensation expense related to unvested 2016 and 2017 performance-based restricted stock unit awards at March 31, 2018. Unrecognized compensation expense related to unvested 2018 performance-based restricted stock units was $21.1 million at March 31, 2018, based on the probable performance target at that date, which is expected to be recognized as expense over the weighted average period of 3.7 years.

Employee Stock Purchase Plan

Under the Company's 2010 Employee Stock Purchase Plan ("ESPP"), eligible employees are granted the right to purchase shares at the lower of 85% of the fair market value of the stock at the time of grant or 85% of the fair market value at the time of exercise. The right to purchase shares is granted twice yearly for six month offering periods in June and December and exercisable on or about the succeeding December and June, respectively, on each year.

Stock-Based Compensation

Stock-based compensation expense related to stock options, restricted stock units, the ESPP and performance-based restricted stock units is included in the following line items in the accompanying Condensed Consolidated Statements of Operations for the three months ended March 31, 2018 and 2017 (in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Cost of revenue | $1,002 | $1,210 |
| Sales and marketing | 6,246 | 6,754 |
| Research and development | 2,308 | 2,102 |
| General and administrative | 4,487 | 5,783 |
| Restructuring | 5,436 | — |
| Total | $19,479 | $15,849 |

8. INCOME TAXES

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (the “Tax Act”) was signed into law making significant changes to the Internal Revenue Code of 1986, as amended. The Tax Act did not result in any material tax expense during three months ended March 31, 2018.

The Company’s income tax provision was approximately $0.5 million with an effective income tax rate of (3.4)% for the three months ended March 31, 2018. The Company’s income tax provision was approximately $0.6 million with an effective income tax rate of (3.7)% for the three months ended March 31, 2017. The Company’s effective tax rate differs from the statutory rate primarily due to the change in the valuation allowance on the Company’s deferred tax assets and foreign income taxes.

The income tax provision is related to domestic income, certain foreign income and withholding taxes. We do not have a material tax provision in the significant jurisdictions we operate in, such as the United States and United Kingdom, as we have historically generated losses. We have recorded a full valuation allowance against the Company’s net deferred tax assets and we do not currently anticipate recording an income tax benefit related to these deferred tax assets or current year losses. The Company will reassess the realization of deferred tax assets each reporting period and will be able to reduce the valuation allowance to the extent that the financial results of these operations improve and it becomes more likely than not that the deferred tax assets are realizable.

The Company is subject to United States federal income tax as well as to income tax in multiple state and foreign jurisdictions, including the United Kingdom. Federal income tax returns of the Company are subject to IRS examination for the 2014 through 2017 tax years. State income tax returns are subject to examination for the 2013 through 2017 tax years. Foreign income tax returns are subject to examination for the 2007 through 2017 tax years. The Company believes it is reasonably possible that within the next twelve months we may resolve certain matters related to the years under examination, which may result in reductions of our unrecognized tax benefits and income tax expense of up to $1.1 million.

At March 31, 2018, we were not able to reasonably estimate, and therefore have not recorded, deferred taxes for the Global Intangible Low-Taxed Income (“GILTI”) provisions. We have not yet determined our policy election with respect to whether to record deferred taxes for basis differences expected to reverse as a result of the GILTI provisions in future periods or use the period cost method. We have, however, included an estimate of the current GILTI impact in our tax provision for 2018.

9. RESTRUCTURING COSTS

In December 2017, as part of the Company's new strategic plan to focus on recurring revenue growth and increase operating margins, the Company approved a restructuring plan to reduce the headcount of the Company's global service delivery team, as well as the headcount of some of its sales teams, representing a total workforce reduction of approximately six percent. The restructuring is part of the Company's renewed focus on recurring, or subscription-based, revenue growth and driving cost reductions to accelerate the growth of its operating margins and free cash flow.

During the three months ended March 31, 2018, the Company continued with strategic plan with the reduction of the professional service headcount, resulting in $7.7 million of restructuring expense which was recorded in "Restructuring" in the accompanying Consolidated Statements of Operations. The restructuring expense consisted primarily of stock-based compensation expense of $5.4 million and $2.3 million of payroll-related costs, such as severance, outplacement costs and continuing healthcare coverage, associated with employee terminations. The stock-based compensation expense relates to accelerated vesting for impacted employees. As of March 31, 2018, the Company incurred an aggregate total of $9.2 million of restructuring expense since the December 2017, which consisted primarily of stock-based compensation expense of $5.5 million and $3.7 million of payroll related costs.

10. COMMITMENTS AND CONTINGENCIES

Guarantees and Indemnifications

The Company has made guarantees and indemnities under which it may be required to make payments to a guaranteed or indemnified party, in relation to certain transactions, including revenue transactions in the ordinary course of business. The Company is obligated to indemnify its directors and officers to the maximum extent permitted under the laws of the State of Delaware. However, the Company has a directors and officers insurance policy that may reduce its exposure in certain circumstances and may enable it to recover a portion of future amounts that may be payable, if any. The duration of the guarantees and indemnities varies and, in many cases, is indefinite but subject to statutes of limitations. To date, the Company has made no payments related to these guarantees and indemnities. The Company estimates the fair value of its indemnification obligations as insignificant based on this history and the Company's insurance coverage and therefore has not recorded any liability for these guarantees and indemnities in the accompanying condensed consolidated balance sheets.

Litigation

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business. If the Company determines that it is probable that a loss has been incurred and the amount is reasonably estimable, the Company will record a liability. The Company has determined that it does not have a potential liability related to any legal proceedings or claims that would individually or in the aggregate materially adversely affect its financial condition or operating results.

11. RELATED PARTY TRANSACTIONS

The Cornerstone OnDemand Foundation (the "Foundation") empowers communities in the United States and internationally by increasing the impact of the non-profit sector through the utilization of human capital management technology including the Company's products. The Company's chief executive officer is on the board of directors of the Foundation. The Company does not direct the Foundation's activities, and accordingly, the Company does not consolidate the Foundation's statement of activities with its financial results. During the three months ended March 31, 2018 and 2017, the Company provided at no charge certain resources to the Foundation, with approximate values of $0.8 million and $0.8 million, respectively.

12. SUBSEQUENT EVENTS

The Compensation Committee granted performance-based restricted stock units during April 2018. Achievement of the probable target level would result in the issuance of 57,144 shares of the Company's common stock upon the vesting of the restricted stock units and achievement of the maximum target would result in the issuance of 142,860 shares of the Company's common stock upon the vesting of the restricted stock units. The performance-based restricted stock units will generally vest over five years.

During April and May 2018, the Compensation Committee granted restricted stock units covering an aggregate of 400,626 shares of the Company's common stock which generally vest annually over four years.

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

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements are any statements that look to future events and consist of, among other things, statements regarding our business strategies; anticipated future operating results and operating expenses; our ability to attract new clients to enter into subscriptions for our solutions; our ability to service those clients effectively and induce them to renew and upgrade their deployments of our solutions; our ability to expand our sales organization to address effectively the new industries, our ability to optimize the efficiency of our operations and scalability of our business; geographies and types of organizations we intend to target; our ability to accurately forecast revenue and appropriately plan our expenses; market acceptance of enhancements to our solutions; alternate ways of addressing human capital management needs or new technologies generally by us and our competitors; continued acceptance of SaaS as an effective method for delivering human capital management solutions and other business management applications; the attraction and retention of qualified employees and key personnel; our ability to protect and defend our intellectual property; costs associated with defending intellectual property infringement and other claims; events in the markets for our solutions and alternatives to our solutions, as well as in the United States and global markets generally; future regulatory, judicial and legislative changes in our industry; the timing and amount of capital expenditures and share repurchases; and changes in the competitive environment in our industry and the markets in which we operate. In addition, forward-looking statements also consist of statements involving trend analyses and statements including such words as "may," "believe," "could," "anticipate," "would," "might," "plan," "expect," and similar expressions or the negative of such other comparable terminology. These forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q and are subject to business and economic risks. As such, our actual results could differ materially from those set forth in the forward-looking statements as a result of the factors set forth below in Part II, Item 1A, "Risk Factors," and in our other reports filed with the Securities and Exchange Commission. We assume no obligation to update the forward-looking statements to reflect events that occur or circumstances that exist after the date on which they were made.

The following discussion should be read in conjunction with our unaudited condensed consolidated financial statements and notes thereto appearing elsewhere in this Quarterly Report on Form 10-Q.

Overview

Cornerstone is a leading global provider of learning and human capital management software, delivered as Software-as-a-Service ("SaaS"). We are one of the world's largest cloud computing companies with approximately 36.0 million users across 3,280 clients in 192 countries and 43 different languages. We help organizations around the globe recruit, train and manage their employees.

Following a strategic review process undertaken by our board of directors during 2017, the board determined that the optimal way to maximize shareholder value is to execute a plan to transform our operations and support that plan with a capital infusion and new strategic partnerships. As a result, we entered into an agreement with Silver Lake, one of the world's leading technology private equity investors, and LinkedIn, under which Silver Lake and LinkedIn invested $300.0 million in Cornerstone in the form of convertible senior notes. In November 2017, we announced our strategic plan with the objective of better positioning us for long-term growth and increasing shareholder value. Our plan is to (i) sharpen our focus on recurring revenue growth; (ii) drive operating margin and free cash flow improvement; (iii) develop new recurring revenue streams, including e-learning content subscriptions; (iv) bolster our leadership team; and (v) strengthen our governance to help us best execute on this strategic transformation.

Our human capital management platform combines the world's leading unified talent management solutions with state-of-the-art analytics and HR administration solutions to enable organizations to manage the entire employee lifecycle. Our focus on continuous learning and development helps organizations to empower employees to realize their potential and drive success.

We work with clients across all geographies, verticals and market segments. Our clients include multi-national corporations, large domestic and foreign-based enterprises, mid-market companies, public sector organizations, healthcare providers, higher education institutions, non-profit organizations and small businesses. We sell our platform domestically and internationally through both direct and indirect channels, including direct sales teams

throughout North and South America, Europe and Asia-Pacific and distributor relationships with payroll companies, human resource consultancies and global system integrators.

Our enterprise human capital management platform is composed of four product suites:

- Our Recruiting suite helps organizations to source and attract candidates, assess and select applicants, onboard new hires and manage the entire recruiting process;

- Our Learning suite enables clients to manage training and development programs, knowledge sharing and collaboration among employees, track compliance requirements and support career development for employees. Our content offering delivers fresh, modern content, fueling employee curiosity and inspiring growth;
- Our Performance suite provides tools to manage goal setting, performance reviews, competency assessments, development plans, continuous feedback, compensation management and succession planning; and
- Our HR Administration suite supports employee records administration, organizational management, employee and manager self-service, workforce planning and compliance reporting.

Our clients can supplement the product suites with our state-of-the-art analytics capabilities to make more-informed decisions using data from across the platform for talent mobility, engagement and development so that HR and leadership can focus on strategic initiatives to help their organization succeed.

In addition to our enterprise human capital management platform, we offer Cornerstone PiiQ, formerly known as Cornerstone Growth Edition, which is a cloud-based talent management solution with performance and learning products targeted to organizations with 500 or fewer employees. We currently do not include the number of clients and users of our Cornerstone for Salesforce and Cornerstone PiiQ products in our client and user count metrics as they are not significant and we believe the client and user count metrics for our human capital management platform give a better indication of our overall performance.

Our Client Success team supports our clients' ongoing optimization of their talent processes and use of our platform. In addition, our Cornerstone Edge solutions allow our clients and partners to more easily integrate with a growing marketplace of service providers. After the initial purchase of our platform, we continue to market and sell to our existing clients, who may renew their subscriptions, add additional products, broaden the deployment of the platform across their organizations and increase usage of the platform over time.

We generate most of our revenue from the sale of our products pursuant to multi-year client agreements. Client agreements for our human capital management platform typically have terms of three years. Our sales processes are typically competitive, and sales cycles generally vary in duration from two to nine months depending on the size of the potential client. We generally price our human capital management platform based on the number of products purchased and the permitted number of users with access to each product.

We sell our products through our direct sales teams and, to a lesser extent, indirectly through our distributors. We intend to continue to invest in our direct sales and distribution activities to address our market opportunity.

We generally recognize revenue from subscriptions ratably over the term of the client agreement and revenue from professional services as the services are performed. In certain instances, our clients request enhancements to the underlying features and functionality of our human capital management platform, and in these instances, revenue from subscriptions is recognized over the remaining term of the agreement once access to the enhanced features is made available to the client. We generally invoice our clients upfront for annual subscription fees for multi-year subscriptions and upfront for professional services. We record amounts invoiced for annual subscription periods that have not occurred or services that have not been performed as deferred revenue on our balance sheet. With the growth in the number of clients, our revenue grew to $133.1 million for the three months ended March 31, 2018, respectively, from $111.6 million for the three months ended March 31, 2017, respectively.

We have historically experienced seasonality in terms of when we enter into client agreements. We usually sign a significantly higher percentage of agreements with new clients, as well as renewal agreements with existing clients, in the fourth quarter of each year. In addition, within a given quarter, we typically sign a large portion of these agreements during the last month, and often the last two weeks, of that quarter. We believe this seasonality is driven by several factors, most notably the tendency of procurement departments at our enterprise clients to purchase technology at the end of a quarter or calendar year, possibly in order to use up their available quarterly or annual funding allocations. As the terms of most of our client agreements are full year increments, agreements initially entered into the fourth quarter or last month of any quarter will generally come up for renewal at that same time in subsequent years. This seasonality is reflected to a much lesser extent, and sometimes is not immediately apparent, in our revenue, due to the fact that we recognize subscription revenue over the term of the client agreement, which is generally three years. In addition, this seasonality is reflected in changes in our deferred revenue balance, which generally is impacted by the timing of when we enter into agreements with new clients, invoice new clients, invoice

existing clients for annual subscription periods and recognize revenue. We expect this seasonality to continue, which may cause fluctuations in certain of our operating results and financial metrics, and thus limit our ability to predict future results.

We believe the market for human capital management remains large and underpenetrated, providing us with significant growth opportunities. We expect businesses and other organizations to continue to increase their spending on human capital management platforms in order to maximize the productivity of their employees, manage changing workforce demographics and ensure compliance with global regulatory requirements. Historically, many of these software solutions have been human resource applications running on hardware located on organizations' premises. We have seen many of these organizations increasingly choose SaaS for their human capital management platform and we anticipate that trend will continue.

We have focused on growing our business to pursue what we believe is a significant market opportunity, and we plan to continue to invest in building for growth. As a result, we expect our cost of revenue and operating expenses to increase in future periods. Over time, we expect our sales and marketing expenses to increase, as we continue to expand our direct sales teams, increase our marketing activities and grow our international operations; however, we are focused on optimizing our investment in sales and marketing and expect to obtain operating leverage into future years similar to what we have achieved over the last couple of years. Research and development expenses are expected to increase as we continue to improve the existing functionality for our products. We also believe that we must invest in maintaining a high degree of client service and support that is critical for our continued success. We plan to continue our policy of implementing best practices across our organization, expanding our technical operations and investing in our network infrastructure and service capabilities in order to support continued future growth. While we expect to increase our level of investment in the business, we also expect that these increased levels of spending will drive improved profitability over time, such that we should obtain incremental leverage in categories like general and administrative expenses.

Our quarterly operating results have fluctuated in the past and may continue to fluctuate in the future based on a number of factors, many of which are beyond our control, including those described in the "Risk Factors" section of this Quarterly Report on Form 10-Q. One or more of these factors may cause our operating results to vary widely. As such, we believe that our quarterly results of operations may vary significantly in the future and that period-to-period comparisons of our operating results may not be meaningful and should not be relied upon as an indication of future performance.

Metrics

We regularly review a number of metrics, including the following key metrics, to evaluate our business, measure our performance, identify trends affecting our business, formulate financial projections and make strategic decisions.

- Revenue. We generally recognize subscription revenue over the contract period, and as a result of our revenue recognition policy and the seasonality of when we enter into new client agreements, revenue from client agreements signed in the current period may not be fully reflected in the current period.
- Subscription revenue. Revenue as defined above on a recurring basis.
- Unlevered Free cash flow. We define unlevered free cash flow, a non-GAAP financial measure, as cash provided by operating activities minus capital expenditures and capitalized software costs plus cash paid for interest. We present this metric because it is a liquidity measure that provides useful information to management and investors about the amount of cash generated by our business that can be used for strategic opportunities, including investing in our business and strengthening our balance sheet.
- Constant currency results. We present constant currency information, a non-GAAP financial measure, to provide a framework for assessing how our underlying business performed excluding the effect of foreign currency fluctuations. Due to our legal and operating structure, our international revenues are favorably impacted as the U.S. Dollar weakens relative to the British pound and Euro, and unfavorably impacted as the U.S. Dollar strengthens relative to the British pound and Euro. We believe the presentation of results on a constant currency basis in addition to reported results helps improve the ability to understand our performance because they exclude the effects of foreign currency volatility that are not indicative of our core operating results. To present this information, current period results for entities reporting in British pounds and Euros are translated into U.S. Dollars at the prior period exchange rates as opposed to the actual exchange rates in effect for the current period. These results should be considered in addition to, not as a substitute for, results reported in accordance with GAAP. Results on a constant currency basis, as we present them, may not be comparable to similarly titled measures used by other companies and are not a measure of

performance presented in accordance with GAAP.

- Number of clients. We believe that our ability to expand our client base is an indicator of our market penetration and the growth of our business as we continue to invest in our direct sales teams and distributors. Our client count includes contracted clients for our enterprise human capital management platform as of the end of the period and excludes clients of our Cornerstone for Salesforce and Cornerstone PiiQ products.

- Number of users. Since our clients generally pay fees based on the number of users of our products within their organizations, we believe the total number of users is an indicator of the growth of our business. Our user count includes active users for our enterprise human capital management platform and excludes users of our Cornerstone for Salesforce and Cornerstone PiiQ products.

Key Components of Our Results of Operations

Sources of Revenue and Revenue Recognition

Our platform is designed to enable organizations to meet the challenges they face in maximizing the productivity of their human capital. We generate revenue from the following sources:

- Subscriptions to Our Products and Other Offerings on a Recurring Basis. Clients pay subscription fees for access to our enterprise human capital management platform, other products and support on a recurring basis. Fees are based on a number of factors, including the number of products purchased, which may include e-learning content, and the number of users having access to a product. We generally recognize revenue from subscriptions ratably over the term of the agreements beginning on the date the subscription service is made available to the client. Subscription agreements are typically three years, billed annually in advance, and non-cancelable.
- Professional Services and Other. We offer our clients and implementation partners assistance in implementing our products and optimizing their use. Professional services include application configuration, system integration, business process re-engineering, change management and training services. Services are generally billed upfront on a fixed fee basis and to a lesser degree on a time-and-material basis. These services are generally purchased as part of a subscription arrangement and are typically performed within the first several months of the arrangement. Clients may also purchase professional services at any other time. We generally recognize revenue from fixed fee professional services contracts as services are performed based on the proportion performed to date relative to the total expected services to be performed. Revenue associated with time-and-material contracts are recorded as such time-and-materials are incurred.

Our client agreements generally include both subscription to access our products and related professional services. Our agreements generally do not contain any cancellation or refund provisions other than in the event of our default.

Cost of Revenue

Cost of revenue consists primarily of costs related to hosting our products; personnel and related expenses, including stock-based compensation, for network infrastructure, IT support, delivery of contracted professional services and on-going client support; payments to external service providers contracted to perform implementation services; depreciation of data centers; amortization of capitalized software costs; amortization of developed technology and software license rights; content and licensing fees; and referral fees. In addition, we allocate a portion of overhead, such as rent, IT costs, depreciation and amortization and employee benefits costs, to cost of revenue based on headcount. The costs associated with providing professional services are significantly higher, as a percentage of revenue, than the costs associated with providing access to our products due to the labor costs to provide the consulting services. We expect gross margin to increase over time as we optimize the efficiency of our operations, continue to scale our business and deemphasize the sale of professional services.

Operating Expenses

Our operating expenses are as follows:

- Sales and Marketing. Sales and marketing expenses consist primarily of personnel and related expenses for our sales and marketing staff, including salaries, benefits, bonuses, stock-based compensation and commissions; costs of marketing and promotional events, corporate communications, online marketing, product marketing and other brand-building activities; and allocated overhead.

We intend to continue to invest in sales and marketing strategically to expand our business both domestically and internationally. We expect over time sales and marketing expenses, as a percentage of revenue, to decrease.

- Research and Development. Research and development expenses consist primarily of personnel and related expenses for our research and development staff, including salaries, benefits, bonuses and stock-based compensation; the cost of certain third-party service providers; and allocated overhead. Research and development costs, other than software development costs qualifying for capitalization, are expensed as incurred.

We have focused our research and development efforts on continuously improving our products. We believe that our research and development activities are efficient because we benefit from maintaining a single software code base for each of our products. We expect research and development expenses to increase proportionately with our business.

- General and Administrative. General and administrative expenses consist primarily of personnel and related expenses for administrative, legal, finance and human resource staff, including salaries, benefits, bonuses and stock-based compensation; professional fees; insurance premiums; other corporate expenses; and allocated overhead. We expect our general and administrative expenses to increase in absolute dollars but decrease as a percentage of revenue.
- Restructuring. Restructuring consists of stock-based compensation, payroll-related costs, such as severance, outplacement costs and continuing healthcare coverage, associated with employee terminations.
- Amortization of Certain Acquired Intangible Assets. Amortization of certain acquired intangible assets consists of amortization of acquisition-related intangibles for customer relationships.

Other Income (Expense)

- Interest Income. Interest income consists primarily of interest income from investment securities partially offset by amortization of investment premiums. We expect interest income to vary depending on the level of our investments in marketable securities, which include corporate bonds, agency bonds, U.S. treasury securities and commercial paper.
- Interest Expense. Interest expense consists primarily of interest expense from our convertible notes, accretion of debt discount and amortization of debt issuance costs.
- Other, Net. Other, net consists of income and expense associated with fluctuations in foreign currency exchange rates, fair value adjustments to strategic investments and other non-operating expenses. We expect other income (expense) to vary depending on the movement in foreign currency exchange rates and the related impact on our foreign exchange gain (loss).

Income Tax (Provision) Benefit

The income tax provision is related to foreign income, state income and withholding taxes. Given our historical losses, we have not recorded a provision, except for state minimum taxes and withholding taxes, for United States, United Kingdom, New Zealand, Hong Kong and Brazil income taxes as we have recorded a full valuation allowance against the net deferred tax assets for each of these countries. Other foreign subsidiaries and branches provide intercompany services and are compensated on a cost-plus basis, and therefore, have incurred liabilities for foreign income taxes in their respective jurisdictions.

Critical Accounting Policies and Estimates

Information with respect to our critical accounting policies that we believe have the most significant effect on our reported results and require subjective or complex judgments of management are contained in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of our Annual Report on Form 10-K filed with the Securities and Exchange Commission, or SEC, on February 27, 2018.

For information regarding recent changes to our critical accounting policies, refer to Note 1 of Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Recent Accounting Pronouncements

For information regarding recent accounting pronouncements, refer to Note 1 of Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Results of Operations

The following table sets forth our results of operations for each of the periods indicated (in thousands). The period-to-period comparison of financial results is not necessarily indicative of future results. The adoption of ASC 606 had an inconsequential impact on the comparability of our financial results for the periods ended March 31, 2018 and 2017.

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 * | 2017 |
| Revenue | $133,113 | $111,582 |
| Cost of revenue | 37,020 | 33,949 |
| Gross profit | 96,093 | 77,633 |
| Operating expenses: | | |
| Sales and marketing | 59,245 | 56,894 |
| Research and development | 15,984 | 13,411 |
| General and administrative | 21,985 | 20,476 |
| Restructuring | 7,725 | — |
| Total operating expenses | 104,939 | 90,781 |
| Loss from operations | (8,846) | (13,148) |
| Other income (expense): | | |
| Interest income | 1,819 | 613 |
| Interest expense | (8,700) | (3,302) |
| Other, net | 44 | 197 |
| Other income (expense), net | (6,837) | (2,492) |
| Loss before income tax provision | (15,683) | (15,640) |
| Income tax provision | (533) | (571) |
| Net loss | $(16,216) | $(16,211) |

The following table sets forth our results of operations as a percentage of total revenue for each of the periods indicated.

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 * | 2017 |
| Revenue | 100.0 % | 100.0 % |
| Cost of revenue | 27.8 % | 30.4 % |
| Gross profit | 72.2 % | 69.6 % |
| Operating expenses: | | |
| Sales and marketing | 44.5 % | 51.0 % |
| Research and development | 12.0 % | 12.0 % |
| General and administrative | 16.5 % | 18.4 % |
| Restructuring | 5.8 % | — % |
| Total operating expenses | 78.8 % | 81.4 % |
| Loss from operations | (6.6)% | (11.8)% |
| Other income (expense): | | |
| Interest income | 1.4 % | 0.5 % |
| Interest expense | (6.5)% | (3.0)% |
| Other, net | — % | 0.2 % |
| Loss before income tax provision | (11.8)% | (14.0)% |
| Income tax provision | (0.4)% | (0.5)% |
| Net loss | (12.2)% | (14.5)% |

*See Note 1 for summary of adjustments.

The following table sets forth our revenue and key metrics that we use to evaluate our business, measure our performance, identify trends affecting our business, formulate financial projections and make strategic decisions:
Metrics

| | At or For Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Revenue (in thousands) | $ 133,113 | $ 111,582 |
| Subscription revenue (in thousands) | $ 113,134 | $ 92,932 |
| Unlevered free cash flow (in thousands) | $ (10,178) | $ (13,791) |
| Number of clients | 3,280 | 2,998 |
| Number of users (in millions) | 36.0 | 31.0 |

Revenue increased by $21.5 million, or 19%, for the three months ended March 31, 2018 as compared to the same period in 2017. Revenue growth on a constant currency basis was 15.1% for the three months ended March 31, 2018 as compared to the same period in 2017. The rate of our revenue increase can be impacted by the mix and timing of new client agreements signed, the success of our focus on recurring revenue and reducing our professional services business, fluctuations in foreign exchange rates, as well as the growth rate of our emerging markets.
The following table sets forth our sources of revenue for each of the periods indicated (dollars in thousands):

| | Three Months Ended March 31, | | | |
|---|---|---|---|---|
| | 2018 | | 2017 | |
| Subscription revenue | $113,134 | | $92,932 | |
| Percentage of subscription revenue to total revenue | 85.0 | % | 83.3 | % |
| Professional services revenue | $19,979 | | $18,650 | |
| Percentage of professional services to total revenue | 15.0 | % | 16.7 | % |
| | $133,113 | | $111,582 | |

Subscription revenue increased by $20.2 million, or 22%, for the three months ended March 31, 2018 as compared to the same period in 2017. Subscription revenue growth on a constant currency basis was 17.8% for the three months ended March 31, 2018 as compared to the same period in 2017. The increase was attributable to new business, which includes new clients, upsells and renewals from existing clients. Professional services revenue increased by $1.3 million, or 7% for the three months ended March 31, 2018 as compared to the same period in 2017. The lower level of growth of professional services revenue is attributed to the continued execution of the strategic initiative announced in the fourth quarter of 2017, which is to sharpen our focus on recurring revenue growth and migrate much of our implementation services to our global partners.
Revenue by geography is generally based on the address of the customer as defined in our master subscription agreement with each customer. The following table sets forth our revenue by geographic area for each of the periods indicated (dollars in thousands):

| | Three Months Ended March 31, | | | |
|---|---|---|---|---|
| | 2018 | | 2017 | |
| Revenue for United States | $82,747 | | $74,800 | |
| Percentage of total revenue for United States | 62.2 | % | 67.0 | % |
| Revenue for all other countries | $50,366 | | $36,782 | |
| Percentage of total revenue for all other countries | 37.8 | % | 33.0 | % |
| | $133,113 | | $111,582 | |

Unlevered free cash flow for the three months ended March 31, 2018 was $(10.2) million, resulting in an unlevered cash flow margin of (7.6)%, as compared to unlevered free cash flow of $(13.8) million and unlevered cash flow margin of (12.4)% for the same period in 2017. We define unlevered free cash flow, a non-GAAP financial measure, as net cash provided by operating activities minus capital expenditures and capitalized software costs plus cash paid for interest. We present this metric because it is a liquidity measure that provides useful information to management and investors about the amount of cash generated by our business that can be used for strategic opportunities, including investing in our business and strengthening our balance sheet.

Our number of clients grew 9% at March 31, 2018 compared to March 31, 2017 and our number of users increased 16% at March 31, 2018 compared to March 31, 2017.

Cost of Revenue, Gross Profit and Gross Margin

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| | (dollars in thousands) | |
| Cost of revenue | $37,020 | $33,949 |
| Gross profit | $96,093 | $77,633 |
| Gross margin | 72.2 % | 69.6 % |

Cost of revenue increased $3.1 million, or 9% for the three months ended March 31, 2018 as compared to the same period in 2017. The increase in cost of revenue was primarily due to $2.6 million in increased third-party implementation costs. The improvement in gross margin was primarily due to a higher mix of subscription revenue, which carry a higher gross margin. Aside from the improvement in gross margin from the higher mix of subscription revenue, we expect gross margin to increase over time as we optimize the efficiency of our operations and continue to scale our business.

Sales and Marketing

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| | (dollars in thousands) | |
| Sales and marketing | $59,245 | $56,894 |
| Percent of revenue | 44.5 % | 51.0 % |

Sales and marketing expenses increased $2.4 million, or 4% for the three months ended March 31, 2018 as compared to the same period in 2017. As a percentage of revenue, sales and marketing expense decreased, primarily resulting from a combination of increased cost efficiency and leverage realized from changes to our sales commission plans, as we continued our efforts to strategically scale our sales teams and improve their productivity.

We assess our investments in new and existing markets strategically and we believe we have gained leverage through our operational excellence initiatives. We expect over time sales and marketing expense, as a percentage of revenue, to continue to decrease as we gain efficiency throughout the various sales teams.

Research and Development

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| | (dollars in thousands) | |
| Research and development | $15,984 | $13,411 |
| Percent of revenue | 12.0 % | 12.0 % |

Research and development expenses increased by $2.6 million, or 19%, for the three months ended March 31, 2018 as compared to the same period in 2017. The increase was principally due to an increase in research and development headcount to maintain and improve the functionality of our products. As a result, we incurred increased employee-related costs of $3.1 million.

We continue to develop and release new products and new features within existing products and as a result, we expect research and development expense to increase proportionately with revenue.

We capitalize a portion of our software development costs related to the development and enhancements of our products, which are then amortized to cost of revenue. The timing of our capitalizable development and enhancement projects may affect the amount of development costs expensed in any given period. We capitalized $7.2 million and $6.0 million of software development costs and amortized $5.3 million and $3.9 million in the three months ended March 31, 2018 and 2017, respectively.

General and Administrative

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| | (dollars in thousands) | |
| General and administrative | $21,985 | $20,476 |
| Percent of revenue | 16.5 % | 18.4 % |

General and administrative expenses increased by $1.5 million, or 7%, for the three months ended March 31, 2018 as compared to the same period in 2017. The increase was largely driven by higher costs to support our growing business and incremental spend to support our operational excellence initiatives, which we expect to result in future margin improvements.

We expect over time our general and administrative expense to increase in absolute dollars but decrease as a percentage of revenue.

Restructuring

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| | (in thousands) | |
| Restructuring | $ 7,725 | $ — |
| Percent of revenue | 5.8 % | —% |

Restructuring expenses of $7.7 million were recorded in the three months ended March 31, 2018, which consisted primarily of payroll-related costs, such as stock compensation, severance, outplacement costs and continuing healthcare coverage, associated with employee terminations. As of March 31, 2018, the Company incurred an aggregate total of $9.2 million of restructuring expense since the December 2017, which consisted primarily of stock-based compensation expense of $5.5 million and $3.8 million of payroll related costs.

Other Income (Expense)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| | (in thousands) | |
| Interest income | $ 1,819 | $ 613 |
| Interest expense | (8,700) | (3,302) |
| Other, net | 44 | 197 |
| Total | $ (6,837) | $ (2,492) |

Interest income for the three months ended March 31, 2018 increased $1.2 million due to the increase in interest income earned on the increased cash balance in the money market account.

Interest expense for the three months ended March 31, 2018 increased by $5.4 million, due to an increase in interest expense for our convertible notes. Refer to the section titled “Liquidity and Capital Resources” below for additional information on the convertible notes.

Other, net is primarily comprised of foreign exchange gains and losses related to transactions denominated in foreign currencies and foreign exchange gains and losses related to our intercompany loans and certain cash accounts. Foreign exchange gains and losses for the three months ended March 31, 2018 and 2017, respectively, were primarily driven by fluctuations in the Euro and U.S. Dollar in relation to the British Pound.

Income Tax Provision

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| | (in thousands) | |
| Income tax provision | $ (533) | $ (571) |

For the three and three months ended March 31, 2018, we recorded an income tax provision related to certain foreign and state income taxes.

Liquidity and Capital Resources

At March 31, 2018, our principal sources of liquidity were $413.3 million of cash and cash equivalents, investments in marketable securities of $222.9 million and $114.0 million of accounts receivable. In June 2013, we issued $253 million of 1.5% convertible notes due July 1, 2018 (the “2018 Notes”) and concurrently entered into convertible note hedges and separate warrant transactions. The 2018 Notes mature on July 1, 2018, unless earlier converted. As of the date of this filing, there have not been any elected conversions.

In December 2017, we issued $300.0 million principal amount of 5.75% senior convertible notes due July 1, 2021 (the “2021 Notes”) for a purchase price equal to 98% of the principal amount, to certain entities affiliated with Silver Lake and LinkedIn. Holders of the 2021 Notes may convert their 2021 Notes at any time prior to the close of business on the scheduled trading day immediately preceding the maturity date.

We intend to use our cash for general corporate purposes, including the payment of 2018 Notes when due, potential future acquisitions or other transactions. Depending on certain growth opportunities, we may choose to accelerate investments in sales and marketing, research and development, technology and services, which may require the use of proceeds for such additional expansion and expenditures. Based on our current level of operations and anticipated growth, we believe our future cash flows from operating activities and existing cash and cash equivalents will provide adequate funds for our ongoing operations and general corporate purposes for at least the next twelve months. Our future capital requirements will depend on many factors, including our rate of revenue growth and collections, the level of our sales and marketing efforts, the timing and extent of spending to support product development efforts and expansion into new territories, the timing of introductions of new services and enhancements to existing services, the timing of general and administrative expenses as we grow our administrative infrastructure and the continuing market acceptance of our products. To the extent that existing cash and cash from operations are not sufficient to fund our

future activities, we may need to raise additional funds. In addition, we may enter into agreements or letters of intent with respect to potential investments in, or acquisitions of, complementary businesses, services or technologies in the future, which could also require us to seek additional financing or utilize our cash resources.

The following table sets forth a summary of our cash flows for the periods indicated (in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2018 | 2017 |
| Net cash used by operating activities | $(4,580) | $(7,235) |
| Net cash provided by (used in) investing activities | 32,079 | (20,248) |
| Net cash (used in) provided by financing activities | (8,087) | 3,473 |

Our cash flows from operating activities are significantly influenced by our growth, ability to maintain our contractual billing and collection terms, and our investments in headcount and infrastructure to support anticipated growth. Given the seasonality and continued growth of our business, our cash flows from operations will vary from period to period.

Cash used by operating activities was $4.6 million for the three months ended March 31, 2018 compared to $7.2 million for the three months ended March 31, 2017. The increase in operating cash flow was primarily due to working capital changes in 2018 when compared to 2017.

Our primary investing activities have consisted of investments, capital expenditures to develop our capitalized software as well as to purchase software, computer equipment, leasehold improvements and furniture and fixtures in support of expanding our infrastructure and workforce.

Cash provided by investing activities was $32.1 million for the three months ended March 31, 2018, compared to cash used in investing activities of $20.2 million for the three months ended March 31, 2017. The increase in cash provided by investing activities was primarily due to the decrease in purchases of investments.

Cash used in financing activities was $8.1 million for the three months ended March 31, 2018, compared to cash provided by financing activities of $3.5 million for the three months ended March 31, 2017. The decrease in financing cash flows was primarily due to the repurchases of common stock.

Share Repurchase Program

In November 2017, our board of directors authorized a $100.0 million share repurchase program of our common stock. We may repurchase our common stock for cash in the open market in accordance with applicable securities laws. The timing and amount of any stock repurchase will depend on share price, corporate and regulatory requirements, economic and market conditions, and other factors. The repurchase authorization will expire in November 2019.

The following is a summary of our stock repurchases as of May 4, 2018 (in thousands, except per share information):

| Period | # of Shares Repurchased | Average Price per Share | Total Expenditures |
|---|---|---|---|
| November 8, 2017 - December 31, 2017 | 635 | 35.55 | 22,599 |
| January 1, 2018 - March 31, 2018 | 423 | 37.84 | 16,024 |
| April 1, 2018 - May 4, 2018 | 100 | 39.44 | 3,988 |
| Total | 1,158 | 36.74 | 42,611 |

At March 31, 2018, $61.4 million remained available under the share repurchase program.

Contractual Obligations

There have been no material changes in contractual obligations from those disclosed in our Annual Report on Form 10-K filed with the SEC on February 24, 2018.

Off-Balance Sheet Arrangements

As part of our ongoing business, we do not have any relationships with other entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, that have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. We are therefore not exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in those types of relationships.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

We have operations in the United States and internationally, and we are exposed to market risks in the ordinary course of our business. These risks primarily include interest rate, foreign exchange, inflation and counterparty risks, as well as risks relating to changes in the general economic conditions in the countries where we conduct business. To reduce certain of these risks, we monitor the financial condition of our large clients and limit credit exposure by principally collecting in advance and setting credit limits as we deem appropriate. In addition, our investment strategy has been to invest in financial instruments, including corporate bonds, U.S. treasury securities, agency securities, commercial paper and money market funds backed by United States Treasury Bills within the guidelines established under our investment policy. We also make strategic investments in privately-held companies in the development stage. To date, we have not used derivative instruments to mitigate the impact of our market risk exposures. We have also not used, nor do we intend to use, derivatives for trading or speculative purposes.

Interest Rate Risk

At March 31, 2018, we had cash and cash equivalents of $413.3 million and investments of $225.9 million, which primarily consisted of corporate bonds, U.S. treasury securities, agency securities, commercial paper, money market funds backed by United States Treasury Bills and other debt securities. The carrying amount of our cash equivalents reasonably approximates fair value due to the short maturities of these instruments.

The primary objectives of our investment activities are the preservation of capital, the fulfillment of liquidity needs and the fiduciary control of cash and investments. We do not enter into investments for trading or speculative purposes. Our investments are exposed to market risk due to fluctuations in interest rates, which may affect the fair market value of our investments. An increase of 50-basis points in interest rates would have resulted in a $0.4 million reduction on the fair market value of our portfolio as of March 31, 2018. We therefore do not expect our operating results or cash flows to be materially affected by a sudden change in market interest rates.

We do not believe our cash equivalents, corporate bonds, U.S. treasury securities, agency securities and commercial paper have significant risk of default or illiquidity. While we believe these cash investments do not contain excessive risk, we cannot provide assurance that in the future our investments will not be subject to adverse changes in market value. In addition, we maintain significant amounts of cash and cash equivalents at one or more financial institutions that are in excess of federally insured limits. We cannot provide assurance that we will not experience losses on these deposits.

Foreign Currency Risk

We have foreign currency risks related to our revenue and operating expenses denominated in currencies other than the U.S. Dollar, primarily Euros and British Pounds. To a lesser extent, we also have revenue denominated in Australian Dollars, Brazilian Reals, Canadian Dollars, Chinese Yuan, Hong Kong Dollars, Indian Rupees, Japanese Yen, Mexican Pesos, New Zealand Dollars, Singapore Dollars, South African Rand, Swedish Krona, Swiss Franc and other foreign currencies, and operating expenses denominated in Australian Dollars, Brazilian Reals, Canadian Dollars, Chinese Yuan, Hong Kong Dollars, Indian Rupees, Israeli Shekels, Japanese Yen, Mexican Pesos, New Zealand Dollars, Singapore Dollars and Swedish Krona. Increases and decreases in our foreign-denominated revenue from movements in foreign exchange rates are often partially offset by the corresponding decreases or increases in our foreign-denominated operating expenses. Due to our legal structure, revenue and operating expenses denominated in currencies other than the U.S. Dollar primarily flow through subsidiaries with functional currencies of the British Pound and Euro. Our other income (expense) is also impacted by the remeasurement of U.S. Dollar denominated intercompany loans, cash accounts held by our overseas subsidiaries, accounts receivable denominated in foreign currencies and accounts payable denominated in foreign currencies.

As our international operations grow, our risks associated with fluctuation in currency rates will become greater, and we will continue to reassess our approach to managing this risk. In addition, currency fluctuations or a weakening U.S. Dollar can increase the costs of our international expansion. To date, we have not entered into any foreign currency hedging contracts although we may do so in the future. The effect of an immediate 10% adverse change in foreign exchange rates on foreign-denominated accounts at March 31, 2018, including our intercompany loans with our subsidiaries, would result in a foreign currency loss of approximately $8.1 million.

Inflation Risk

We do not believe that inflation has had a material effect on our business, financial condition or results of operations. Nonetheless, if our costs were to become subject to significant inflationary pressures, we may not be able to fully offset such higher costs through price increases. Our inability or failure to do so could harm our business, financial condition and results of operations.

Counterparty Risk

Our financial statements are subject to counterparty credit risk, which we consider as part of the overall fair value measurement. We attempt to mitigate this risk through credit monitoring procedures.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), refers to controls and procedures 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 such information is accumulated and communicated to a company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

Our management, with the participation of our chief executive officer and chief financial officer, has evaluated the effectiveness of our disclosure controls and procedures as of March 31, 2018, the end of the period covered by this Quarterly Report on Form 10-Q. Based upon such evaluation, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures were effective as of such date.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting that occurred during the three months ended March 31, 2018 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

From time to time, we are involved in a variety of claims, suits, investigations and proceedings arising from the ordinary course of our business, including actions with respect to intellectual property claims, breach of contract and tort claims, labor and employment claims, tax and other matters. Although claims, suits, investigations and proceedings are inherently uncertain and their results cannot be predicted with certainty, we believe that the resolution of our current pending matters will not have a material adverse effect on our business, consolidated financial position, results of operations or cash flow. Regardless of the outcome, litigation can have an adverse impact on us because of defense costs, diversion of management resources and other factors. In addition, it is possible that an unfavorable resolution of one or more such proceedings could in the future materially and adversely affect our financial position, results of operations or cash flows in a particular period.

ITEM 1A. Risk Factors

The following risk factors and other information included in this Quarterly Report on Form 10-Q should be carefully considered. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we presently deem less significant may also impair our business operations. Please see page 18 of this Quarterly Report on Form 10-Q for a discussion of the forward-looking statements that are qualified by these risk factors. If any of the events or circumstances described in the following risk factors actually occurs, our business, operating results and financial condition could be materially adversely affected.

Risks Related to Our Business and Industry

Unfavorable conditions in our industry or the global economy, or reductions in information technology spending, could limit our ability to grow our business and negatively affect our operating results.

Our operating results may vary based on the impact of changes in our industry or the global economy on us or our clients. The revenue growth and potential profitability of our business depends on demand for enterprise application software and services generally and for human capital management platform in particular. We sell our human capital management platform primarily to large, mid-sized and small business organizations whose businesses fluctuate based on general economic and business conditions. In addition, a portion of our revenue is attributable to the number of users of our products at each of our clients, which in turn is influenced by the employment and hiring patterns of our clients and potential clients. To the extent that economic uncertainty or weak economic conditions cause our clients and potential clients to freeze or reduce their headcount, demand for our products may be negatively affected. Historically, economic downturns have resulted in overall reductions in spending on information technology and human capital management platforms as well as pressure from clients and potential clients for extended billing terms. If economic conditions deteriorate, our clients and potential clients may elect to decrease their information technology and human capital management budgets by deferring or reconsidering product purchases, which would limit our ability to grow our business and negatively affect our operating results.

Our financial results may fluctuate due to our long, variable and, therefore, unpredictable sales cycle and our focus on large and mid-market organizations.

We plan our expenses based on certain assumptions about the length and variability of our sales cycle. If our sales cycle becomes longer or more variable, our results may be adversely affected. Our sales cycle generally varies in duration from two to nine months and, in some cases, much longer depending on the size of the potential client. Factors that may influence the length and variability of our sales cycle include among others:

- the need to educate potential clients about the uses and benefits of our products;
- the relatively long duration of the commitment clients make in their agreements with us;
- the discretionary nature of potential clients' purchasing and budget cycles and decisions;
- the competitive nature of potential clients' evaluation and purchasing processes;
- the lengthy purchasing approval processes of potential clients;
- the evolving functionality demands of potential clients;
- fluctuations in the human capital management needs of potential clients; and
- announcements or planned introductions of new products by us or our competitors.

The fluctuations that result from the length and variability of our sales cycle may be magnified by our focus on sales to large and mid-sized organizations. If we are unable to close an expected significant transaction with one or more of these companies in a particular period, or if an expected transaction is delayed until a subsequent period, our operating results for that period, and for any future periods in which revenue from such transaction would otherwise have been recognized, may be adversely affected.

Our financial results may fluctuate due to various business factors, some of which may be beyond our control.

There are a number of other factors that may cause our financial results to fluctuate from period to period, including among others:

- changes in billing cycles and the size of advance payments relative to overall contract value in client agreements;
- the extent to which new clients are attracted to our products to satisfy their human capital management needs;
- the timing and rate at which we sign agreements with new clients;
- our access to service providers and partners when we outsource client service projects and our ability to manage the quality and completion of the related client implementations;

- the timing and duration of our client implementations, which is often outside of our direct control;
- our ability to provide, or partner with effective partners to provide, resources for client implementations and consulting projects;
- the extent to which we retain existing clients and satisfy their requirements;
- the extent to which existing clients renew their subscriptions to our products and the timing of those renewals;
- the extent to which existing clients purchase or discontinue the use of additional products and add or decrease the number of users;
- the extent to which our clients request enhancements to underlying features and functionality of our products and the timing of our delivery of these enhancements to our clients;
- the addition or loss of large clients, including through acquisitions or consolidations;
- the number and size of new clients, as well as the number and size of renewal clients in a particular period;
- the mix of clients among small, mid-sized and large organizations;
- changes in our pricing policies or those of our competitors;
- seasonal factors affecting demand for our products or potential clients' purchasing decisions;
- the financial condition and creditworthiness of our clients;
- the amount and timing of our operating expenses, including those related to the maintenance, expansion and restructuring of our business, operations and infrastructure;
- changes in the operational efficiency of our business;
- the timing and success of our new product and service introductions;
- the timing of expenses of the development of new products and technologies, including enhancements to our products;
- our ability to exploit Big Data to drive increased demand for our products;
- continued strong demand for human capital management in the U.S. and globally;
- our ability to successfully integrate our operations with those of acquired privately-held companies;
- the success of current and new competitive products and services by our competitors;
- other changes in the competitive dynamics of our industry, including consolidation among competitors, clients or strategic partners;
- our ability to manage our existing business and future growth, including in terms of additional headcount, additional clients, incremental users and new geographic regions;
- expenses related to our network and data centers and the expansion of such networks and data centers;
- the effects of, and expenses associated with, acquisitions of third-party technologies or businesses and any potential future charges for impairment of goodwill resulting from those acquisitions;
- equity issuances, including as consideration in acquisitions or due to the conversion of our outstanding convertible notes due 2021 and 2018;
- business disruptions, costs and future events related to shareholder activism;
- legal or political changes in local or foreign jurisdictions that decrease demand for, or restrict our ability to sell or provide, our products;
- fluctuations in foreign currency exchange rates, including any fluctuation caused by uncertainties relating to Brexit;
- general economic, industry and market conditions; and
- various factors related to disruptions in our SaaS hosting network infrastructure, defects in our products, privacy and data security and exchange rate fluctuations, each of which is described elsewhere in these risk factors.

In light of the foregoing factors, we believe that our financial results, including our revenue and deferred revenue levels, may vary significantly from period-to-period. As a result, period-to-period comparisons of our operating results may not be meaningful and should not be relied on as an indication of future performance.

The market in which we participate is intensely competitive, and if we do not compete effectively, our operating results could be harmed.

The market for human capital management software is highly competitive, rapidly evolving and fragmented. Many of our competitors and potential competitors are larger and have greater brand name recognition, much longer operating histories, larger marketing budgets and significantly greater resources than we do. In addition, with the introduction of

new technologies and market entrants, we expect competition to intensify in the future. If we fail to compete effectively, our business will be

harmed. Some of our principal competitors offer their products or services at a lower price, which has resulted in pricing pressures. Similarly, some competitors offer different billing terms, which has resulted in pressures on our billing terms. If we are unable to maintain our pricing levels and billing terms, our operating results could be negatively impacted. In addition, pricing pressures and increased competition generally could result in reduced sales, reduced margins, losses or the failure of our products to achieve or maintain more widespread market acceptance, any of which could harm our business.

We face competition from paper-based processes and desktop software tools. We also face competition from custom-built software that is designed to support the needs of a single organization, as well as from third-party talent and human resource application providers. These software vendors include, without limitation, Halogen Software, Inc., International Business Machines Corporation, Oracle Corporation, Peoplefluent, Inc., Saba Software, Inc., SAP America, Inc., Skillsoft Corp., Talentsoft and Workday, Inc. In addition, some of the parties with which we maintain business alliances offer or may offer products or services that compete with our products or services.

Many of our competitors are able to devote greater resources to the development, promotion and sale of their products and services. In addition, many of our competitors have established marketing relationships, access to larger client bases and major distribution agreements with consultants, system integrators and distributors. Moreover, many software vendors can bundle human resource products or offer such products at a lower price as part of a larger product sale. In addition, some competitors may offer software that addresses one or a limited number of human capital management functions at a lower price point or with greater depth than our products. As a result, our competitors may be able to respond more quickly and effectively than we can to new or changing opportunities, technologies, standards or client requirements. Further, some potential clients, particularly large enterprises, may elect to develop their own internal products. For all of these reasons, we may not be able to compete successfully against our current and future competitors.

Existing or future laws and regulations relating to privacy or data security could increase the cost of our products, limit their use and adoption, and subject us or our clients to litigation, regulatory investigations and penalties and other potential liabilities.

Our human capital management platform enables our clients to collect, manage and store a wide range of data, including personal data, related to every phase of the employee performance and management cycle. The United States and various state governments have adopted or proposed laws governing the collection, use, storage, sharing and processing of personal data. Several foreign jurisdictions, including but not limited to the European Union, (the "EU"), its member states, Korea, Japan, Singapore, Australia and India, have adopted legislation (including directives or regulations) that increase or change the requirements governing the personal data of individuals in these jurisdictions. In some cases, these laws impose obligations not only on many of our clients, but also directly on us. These laws and regulations are complex and change frequently, at times due to differing economic conditions and changes in political climate, with new laws and regulations proposed frequently and existing laws and regulations subject to different and conflicting interpretations. These laws have the potential to increase costs of compliance, risks of noncompliance and penalties for noncompliance and the cost and complexity of selling and delivering our solutions. For example, the EU's General Data Protection Regulation ("GDPR"), which takes effect on May 25, 2018, imposes new obligations on our clients and directly on us as both a data controller of our own employees' data and a data processor of our clients' data. Companies that violate the GDPR can face fines of up to the greater of 20 million Euros or 4% of their worldwide annual turnover. These and other requirements could reduce demand for our services, require us to take on more onerous obligations in our contracts, restrict our ability to store, transfer and process data or, in some cases, impact our ability to offer our services in certain locations or our customers' ability to deploy our solutions globally.

In addition, the mechanisms allowing companies to transfer personal data outside of the European Economic Area ("EEA") face ongoing legal challenges in the EU and threaten our ability to lawfully process personal data where we operate outside of the EEA. One of these challenges has been brought against the EU-US Privacy Shield Framework, which we rely on for transfers of personal data from the EEA to the United States. We also rely on the European Commission's recognition of Israel and New Zealand, where we maintain significant support centers, as providing an "adequate" level of protection for personal data transferred from the EEA to those countries. Finally, we rely on the European Commission's Standard Contractual Clauses for transfers of personal data from the EEA to India, where we

also maintain a significant support center. Loss of our ability to lawfully transfer personal data out of the EEA to these or any other jurisdictions may cause reluctance or refusal by current or prospective European clients to use our products. Further, the United Kingdom's vote in favor of exiting the EU (often referred to as "Brexit") has created uncertainty with regard to the regulation of data protection in the United Kingdom. In particular, it is unclear whether the United Kingdom will enact data protection legislation equivalent to the GDPR and how data transfers to and from the United Kingdom will be regulated after Brexit. We maintain a data center in the United Kingdom where EU residents' personal data is processed, and it is unclear whether this processing will comply with European data protection law after Brexit. We are in the process of building data centers in other EU locations that we anticipate will be functional in 2018, but delays in completing the data centers or impediments to beginning operations may harm our customer retention and sales in Europe. Notwithstanding our investment in EU data centers, they may not resolve all concerns that

European companies have about working with U.S. companies in the current legal climate. Additionally, other countries outside of the EEA have passed or are considering passing laws requiring local data residency.

The costs of compliance with, and other burdens imposed by, privacy and data security laws and regulations may limit the use and adoption of our services, lead to negative publicity, reduce overall demand for our services, make it more difficult to meet expectations of or commitments to customers, lead to significant fines, penalties or liabilities for noncompliance, or slow the pace at which we close sales transactions, any of which could harm our business. Even the perception that the privacy of personal information is not satisfactorily protected or does not meet regulatory requirements could inhibit sales of our products or services and could limit adoption of our solutions.

In addition to government activity, privacy advocacy and other industry groups have established or may establish new self-regulatory standards that may place additional burdens on our ability to provide our services globally. Our customers expect us to meet voluntary certifications and other standards established by third parties, such as ISO27001. If we are unable to earn and maintain these certifications or meet these standards, it could adversely affect our ability to provide our solutions to certain customers and could harm our business.

Furthermore, concerns regarding data privacy and security may cause our customers' customers to resist providing the data necessary to allow our customers to use our services effectively. Even the perception that the privacy of personal information is not satisfactorily protected or does not meet regulatory requirements could inhibit sales of our products or services and could limit adoption of our cloud-based solutions.

Any of these matters could materially adversely affect our business, financial condition or operational results.

Mergers of or other strategic transactions by our competitors could weaken our competitive position or reduce our revenue.

If one or more of our competitors were to merge, acquire or partner with another of our competitors, the change in the competitive landscape could adversely affect our ability to compete effectively. For example, in October 2014, Skillsoft Corp. acquired SumTotal Systems, Inc., and in May 2017, Saba Software, Inc. acquired Halogen Software, Inc. Our competitors may also establish or strengthen cooperative relationships with our current or future strategic distributors, systems integrators, HR outsourcers, payroll services companies, third-party consulting firms or other parties with whom we have relationships, thereby limiting our ability to promote our products and limiting the number of consultants available to implement our products. Disruptions in our business caused by these events could reduce our revenue.

Our business and operations are experiencing growth and organizational change. If we fail to effectively manage such growth and change in a manner that preserves the key aspects of our corporate culture, our business and operating results could be harmed.

We have experienced, and may continue to experience, rapid growth and organizational change, which has placed, and may continue to place, significant demands on our management, operational and financial resources. For example, our headcount has decreased from 1,859 employees on March 31, 2017 to 1,829 employees on March 31, 2018. In addition, we have several international offices, including in Australia, Brazil, France, Germany, Hong Kong, India, Israel, Japan, Netherlands, New Zealand, Spain, Sweden and the United Kingdom. We may continue to expand our international operations into other countries in the future, either organically or through acquisitions. We have also experienced significant growth in the number of users, transactions and data that our SaaS hosting infrastructure supports. Finally, our organizational structure is becoming more complex as we improve our operational, financial and management controls as well as our reporting systems and procedures. We will require significant capital expenditures and the allocation of valuable management resources to grow and change in these areas without undermining our corporate culture of rapid innovation, teamwork and attention to client success that has been central to our growth so far. If we fail to manage our anticipated growth and change in a manner that preserves the key aspects of our corporate culture, the quality of our products may suffer, which could negatively affect our brand and reputation and harm our ability to retain and attract clients.

For a detailed discussion of the risks related to our ability to expand our business internationally, manage growth in our SaaS hosting network infrastructure and expand parts of our organization to implement improved operational, financial and management controls and reporting systems, see the risk factors titled "—As a public company, we are obligated to maintain proper and effective internal control over financial reporting. If our internal control over

financial reporting is ineffective, our financial reporting may not be accurate, complete and timely and our auditors may be unable to attest to its effectiveness when required, thus adversely affecting investor confidence in our company." and "—We currently have a number of international offices and are expanding our international operations. Additionally, we do not have substantial experience in all international markets and may not achieve the results that we expect."

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

We conduct our business in the Americas, Europe, and Asia Pacific. As we continue to expand our international operations, we will become more exposed to the effects of fluctuations in currency exchange rates. This exposure is the result of selling in multiple currencies and operating in foreign countries where the functional currency is the local currency. Further, our overseas subsidiaries' results are also impacted by exchange rates affecting the carrying value of U.S. Dollar denominated intercompany loans with us. Because we conduct business in currencies other than U.S. dollars, but report our results of operations in U.S. dollars, fluctuations in the exchange rates of these foreign currencies, including any fluctuations caused by uncertainties relating to Brexit, may hinder our ability to predict our future results and earnings and materially impact our business, financial condition and operating results. Due to our legal structure, any fluctuations in the exchange rates of the British Pound may be particularly impactful. We have not previously engaged in foreign currency hedging. If we decide to hedge our foreign currency exposure, we may not be able to completely eliminate the impact of fluctuations in the exchange rates.

We may acquire other companies or technologies, which could divert our management's attention, result in additional dilution to our stockholders or otherwise disrupt our operations and harm our operating results.

In April 2012, we acquired Sonar Limited, a SaaS talent management solution provider serving small businesses, and in November 2014, we acquired Evolv Inc., a machine learning and data science platform provider. In the future, we may seek to acquire or invest in other businesses, products or technologies that we believe could complement or expand our existing platform, enhance our technical capabilities or otherwise offer growth opportunities. The pursuit of potential acquisitions may divert the attention of management and cause us to incur various expenses in identifying, investigating and pursuing suitable acquisitions, whether or not they are ultimately consummated.

Other than our acquisitions of Sonar Limited and Evolv Inc., we do not have any experience in acquiring other businesses. We may not be able to successfully integrate the personnel, operations and technologies of any businesses that we have acquired or may acquire in the future or effectively manage the combined business following the acquisition. We may also not achieve the anticipated benefits from other acquired businesses due to a number of factors, including:

- unanticipated costs or liabilities associated with the acquisition;
- incurrence of acquisition-related costs;
- diversion of management's attention from other business concerns;
- harm to our existing relationships with distributors and clients as a result of the acquisition;
- the potential loss of key employees;
- exposure to claims and disputes by third parties, including intellectual property claims and disputes;
- the use of resources that are needed in other parts of our business; and
- the use of substantial portions of our available cash to consummate the acquisition.

In addition, a significant portion of the purchase price of companies we acquire may be allocated to acquired goodwill, which must be assessed for impairment at least annually, or to intangible assets, which are assessed for impairment upon certain triggering events. In the future, if our acquisitions do not yield expected returns, we may be required to take charges to our operating results based on this impairment assessment process, which could harm our operating results.

Acquisitions could also result in dilutive issuances of equity securities or the incurrence of debt, which could adversely affect our operating results. For example, in our acquisition of Sonar Limited, we issued an aggregate of 46,694 shares of our common stock. In addition, if an acquired business fails to meet our expectations, our operating results, business and financial condition may suffer.

As a public company, we are obligated to maintain proper and effective internal control over financial reporting. If our internal control over financial reporting is ineffective, our financial reporting may not be accurate, complete and timely and our auditors may be unable to attest to its effectiveness when required, thus adversely affecting investor confidence in our company.

We are required, pursuant to Section 404 of the Sarbanes-Oxley Act, to furnish a report by management on, among other things, the effectiveness of our internal control over financial reporting. Our auditors also need to audit the effectiveness of our internal control over financial reporting. These assessments need to include disclosure of any material weaknesses in our internal control over financial reporting.

We have incurred and continue to incur significant costs assessing our system of internal control over financial reporting and processing documentation necessary to perform the evaluation needed to comply with Section 404. We may discover, and may not be able to remediate, future significant deficiencies or material weaknesses, or we may be unable to complete our

evaluation, testing or any required remediation in a timely fashion. Failure of our internal control over financial reporting to be effective could cause our financial reporting to be inaccurate, incomplete or delayed. Moreover, even if there is no inaccuracy, incompletion or delay of reporting results, if we identify one or more material weaknesses in our internal control over financial reporting, we will be unable to assert, and our auditors will be unable to affirm, that our internal control is effective, in which case investors may lose confidence in the accuracy and completeness of our financial reports, which could have a material adverse effect on the price of our common stock.

Our systems collect, access, use and store personal and other client proprietary information. As a result, we are subject to security risks and are required to invest significant resources to prevent or correct problems caused by security breaches. If a security breach occurs, our reputation could be harmed, our business may suffer and we could incur significant liability.

Our human capital management platform involves the storage and transmission of clients' sensitive, proprietary and confidential information, including personal information, over the Internet (including public networks). Our security measures may be breached as a result of efforts by individuals or groups of hackers and sophisticated organizations, including state-sponsored organizations or nation-states. Our security measures could also be compromised by employee error or malfeasance, which could result in someone obtaining unauthorized access to, or denying authorized access to our IT systems, our customers' data or our data, including our intellectual property and other confidential business information. Additionally, third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information to gain access to our customers' data, our data or our IT systems.

Such breaches and other incidents can result in a risk of unauthorized, unlawful or inappropriate access to, denial of access to, disclosure of, or loss of our customers' or our sensitive, proprietary and confidential information, as well as damage to our IT systems and our ability to make required reporting and disclosures as a public company. An actual or perceived security breach or similar incident could adversely affect our operating results and financial condition due to loss of confidence in the security of our products, damage to our reputation, early termination of contracts, decline in sales, disruption to our operations, litigation, regulatory investigations and penalties, or other liabilities.

In particular, federal, state and foreign governments continue to adopt new, or modify existing, laws requiring companies and their service providers to maintain certain security measures or to report data breaches to government authorities or affected individuals. In turn, customers' expectations for the security measures we implement have increased. If we experience security breaches that could have been prevented by measures required by these laws or our customer contracts, or fail to report security breaches within timeframes mandated by law or our customer contracts, we could face significant liability.

Techniques to compromise IT systems have become more complex over time and are often not identified until they are exploited. As a result, we may be unable to anticipate or prevent such techniques. Our products operate in conjunction with and are dependent on a broad range of products, components and third party services, and a vulnerability in any of them can expose us to a security breach. In addition, our customers and their third party service providers may not have adequate security measures in place to protect their data that is stored in our platform, and because we do not control our customers or their service providers, we cannot prevent vulnerabilities in their security measures from being exploited.

Our efforts to detect, prevent and remediate known or potential security vulnerabilities, including those arising from third-party hardware or software, may result in additional direct and indirect costs.

Finally, if a high profile security breach occurs with respect to another SaaS provider, our clients and potential clients may lose trust in the security of the SaaS business model generally, which could adversely impact our ability to retain existing clients or attract new ones.

Any significant disruption in our SaaS hosting network infrastructure could harm our reputation, require us to provide credits or refunds, result in early terminations of client agreements or a loss of clients and adversely affect our business.

Our SaaS hosting network infrastructure is a critical part of our business operations. Our clients access our human capital management platform through a standard web browser and depend on us for fast and reliable access to our products. Our software is proprietary, and we currently rely on two third-party data center hosting facilities, which we

lease, and the expertise of members of our engineering and software development teams for the continued performance of our platform. Recently, we began the process of migrating our platform from our leased data center hosting facilities to third-party data center hosting facilities operated by Amazon Web Services ("AWS"). After we complete this migration, we will rely extensively on AWS to provide our clients and their users with fast and reliable access to our products. Any disruption of or interference with our SaaS hosting network infrastructure, including the services and operations of AWS, could harm our reputation, business and results of operations. We have experienced, and may in the future experience, disruptions in our computing and communications infrastructure. Factors that may cause such disruptions that may harm our reputation include:

- human error;
- security breaches;

- telecommunications outages from third-party providers;
- computer viruses;
- acts of terrorism, sabotage or other intentional acts of vandalism, including cyber attacks;
- unforeseen interruption or damages experienced in moving hardware to a new location;
- fire, earthquake, flood and other natural disasters; and
- power loss.

Although we generally back-up our client databases hourly, store our data in more than one geographically distinct location at least weekly and perform real-time mirroring of data to disaster recovery locations, we do not currently offer immediate access to disaster recovery locations in the event of a disaster or major outage. Thus, in the event of any of the factors described above, or certain other failures of our computing infrastructure, clients may not be able to access their data for 24 hours or more and there is a remote chance that client data from recent transactions may be permanently lost or otherwise compromised. In addition, we may not have adequate insurance coverage to compensate for losses from a major interruption. Moreover, some of our agreements include performance guarantees and service level standards that obligate us to provide credits, refunds or termination rights in the event of a significant disruption in our SaaS hosting network infrastructure or other technical problems that relate to the functionality or design of our platform.

Certain of our operating results and financial metrics are difficult to predict as a result of seasonality.

We have historically experienced seasonality in terms of when we enter into client agreements for our products. We sign a significantly higher percentage of agreements with new clients, and renewal agreements with existing clients, in the fourth quarter of each year and a significant portion of these agreements are signed during the last month, and with respect to each quarter, often the last two weeks of the quarter. This seasonality is reflected to a much lesser extent, and sometimes is not immediately apparent, in our revenue, due to the fact that we generally recognize subscription revenue over the term of the client agreement, which is generally three years. We expect this seasonality to continue, which may cause fluctuations in certain of our operating results and financial metrics, and thus difficulties in predictability.

We rely on third-party computer hardware and software that may be difficult to replace or could cause errors or failures of our service.

In addition to the software we develop, we rely on computer hardware, purchased or leased, and software licensed from third parties in order to deliver our platform. This hardware and software may not continue to be available on commercially reasonable terms, if at all. Any loss of the right to use any of this hardware or software could result in delays in our ability to provide our platform until equivalent technology is either developed by us or, if available, identified, obtained and integrated. In addition, errors or defects in third-party hardware or software used in our platform could result in errors or a failure of our products, which could harm our business.

Defects in our platform could affect our reputation, result in significant costs to us and impair our ability to sell our products and related services.

Defects in our platform could adversely affect our reputation, result in significant costs to us and impair our ability to sell our products in the future. The costs incurred in correcting any product defects may be substantial and could adversely affect our operating results. Although we continually test our products for defects and work with clients through our client support organization to identify and correct errors, defects in our products are likely to occur in the future. Any defects that cause interruptions to the availability of our products could result in:

- lost or delayed market acceptance and sales of our products;
- early termination of client agreements or loss of clients;
- credits or refunds to clients;
- product liability suits against us;
- diversion of development resources;
- injury to our reputation; and
- increased maintenance and warranty costs.

While our client agreements typically contain limitations and disclaimers that purport to limit our liability for damages related to defects in our products, such limitations and disclaimers may not be enforced by a court or other tribunal or

otherwise effectively protect us from such claims.

If we fail to manage our SaaS hosting network infrastructure capacity, our existing clients may experience service outages and our new clients may experience delays in the deployment of our human capital management platform.
We have experienced significant growth in the number of users, transactions and data that our hosting infrastructure supports. We seek to maintain sufficient excess capacity in our SaaS hosting network infrastructure to meet the needs of all of our clients. We also seek to maintain excess capacity to facilitate the rapid provision of new client deployments and the expansion of existing client deployments. However, the provision of new hosting infrastructure requires significant lead time. If we do not accurately predict our infrastructure capacity requirements, our existing clients may experience service outages that may subject us to financial penalties, financial liabilities and client losses. If our hosting infrastructure capacity fails to keep pace with increased sales, clients may experience delays as we seek to obtain additional capacity, which could harm our reputation and adversely affect our revenue growth.
Our growth depends in part on the success of our strategic relationships with third parties.
We anticipate that we will continue to depend on various third-party relationships in order to grow our business. In addition to growing our indirect sales channels, we intend to pursue additional relationships with other third parties, such as technology and content providers and implementation consultants. Identifying, negotiating and documenting relationships with third parties require significant time and resources, as does integrating third-party content and technology. Our agreements with distributors and providers of technology, content and consulting services are typically non-exclusive and do not prohibit them from working with our competitors or from offering competing services. Our competitors may be effective in providing incentives to third parties to favor their products or services or to prevent or reduce subscriptions to our products. In addition, these distributors and providers may not perform as expected under our agreements, and we have had and may in the future have, disagreements or disputes with such distributors and providers, which could negatively affect our brand and reputation. A global economic slowdown could also adversely affect the businesses of our distributors and it is possible that they may not be able to devote the resources we expect to our relationships with such distributors.
If we are unsuccessful in establishing or maintaining our relationships with these third parties, our ability to compete in the marketplace or to grow our revenue could be impaired and our operating results could suffer. Even if we are successful, we cannot assure you that these relationships will result in improved operating results.
Failure to effectively retain and expand our direct sales teams and develop and expand our indirect sales channel will impede our growth.
We will need to continue to expand our sales and marketing infrastructure in order to grow our client base and our business. We plan to expand our direct sales teams and engage additional third-party distributors, both domestically and internationally. Identifying, recruiting and training these people and entities will require significant time, expense and attention. Our business will be seriously harmed and our financial resources will be wasted if our efforts to expand our direct and indirect sales channels do not generate a corresponding increase in revenue, and we may be required to sacrifice near-term growth and divert management attention in order to restructure our direct sales teams. In particular, if our recent transition to a sales commission model based solely on subscription or recurring revenue and other recent organizational changes hinder our ability to hire, develop and retain talented sales personnel or if our new direct sales personnel are unable to achieve expected productivity levels in a reasonable period of time, we may not be able to significantly increase our revenue and grow our business.
Restructuring activities could adversely affect our ability to execute our business strategy.
In December 2017, we announced that we were implementing a restructuring plan to reduce the headcount of our global service delivery team, as well as the headcount of some of our sales teams, representing a workforce reduction of approximately six percent. In connection with this action, we incurred approximately $7.7 million of expenditures in the quarter ended March 31, 2018. This restructuring and any future restructurings, should it become necessary for us to continue to restructure our business due to worldwide market conditions or other factors that reduce the demand for our products and services, could adversely affect our ability to execute our business strategy.
If we fail to retain key employees and recruit qualified technical and sales personnel, our business could be harmed.
We believe that our success depends on the continued employment of our senior management and other key employees, such as our chief executive officer. In addition, because our future success is dependent on our ability to continue to enhance and introduce new software and services, we are heavily dependent on our ability to attract and

retain qualified engineers with the requisite education, background and industry experience. As we expand our business, our continued success will also depend, in part, on our ability to attract and retain qualified sales, marketing and operational personnel capable of supporting a larger and more diverse client base. The loss of the services of a significant number of our engineers or sales people could be disruptive to our development efforts or business relationships. In addition, if any of our key employees joins a competitor or

decides to otherwise compete with us, we may experience a material disruption of our operations and development plans, which may cause us to lose clients or increase operating expenses as the attention of our remaining senior managers is diverted to recruit replacements for the departed key employees.

Changes to U.S. immigration and work authorization laws and regulations can be significantly affected by political forces and levels of economic activity. Our international expansion and our business may be materially adversely affected if legislative or administrative changes to immigration or visa laws and regulations impair our hiring processes or projects involving personnel who are not citizens of the country where the work is to be performed.

Failure to effectively manage client deployments by our third-party service providers could adversely impact our business.

In cases where our third-party service providers are engaged either by us or by a client directly to deploy a product for a client, our third-party service providers need to have a substantial understanding of such client's business so that they can configure the product in a manner that complements its existing business processes and integrates the product into its existing systems. It may be difficult for us to manage the timeliness of these deployments and the allocation of personnel and resources by our clients. Failure to successfully manage client deployments by us or our third-party service providers could harm our reputation and cause us to lose existing clients, face potential client disputes or limit the rate at which new clients purchase our products.

Forecasts of our business growth and profitability may prove to be inaccurate, and even if the markets in which we compete achieve the forecasted growth, we cannot assure you our business will grow at similar rates, or at all.

Our forecasts are subject to significant uncertainty and are based on assumptions and estimates which may not prove to be accurate. These assumptions and estimates include the timing and value of agreements with our customers, variability in the service delivery periods for our customers, impact of foreign currency exchange rate fluctuations and expected growth in our market and related costs to support the growth of our business. Our assumptions and estimates related to our business growth and profitability, including the performance of our core business and emerging businesses and the demand for our products in the United States, Europe, Japan and other regions, may prove to be inaccurate. Even if the markets experience the forecasted growth, we may not grow our business at similar rates, or at all. Our growth is subject to many factors, including our success in implementing our business strategy, which is subject to many risks and uncertainties.

Even if demand for human capital management products and services increases generally, there is no guarantee that demand for SaaS products like ours will increase to a corresponding degree.

The widespread adoption of our products depends not only on strong demand for human capital management products and services generally, but also for products and services delivered via a SaaS business model in particular. There are still a significant number of organizations that have adopted no human capital management functions at all, and it is unclear whether such organizations will ever adopt such functions and, if they do, whether they will desire a SaaS human capital management platform like ours. As a result, we cannot assure you that our SaaS human capital management platform will achieve and sustain the high level of market acceptance that is critical for the success of our business.

Our business depends substantially on clients renewing their agreements with us, purchasing additional products from us or adding additional users. Any decline in our clients renewing their agreements, purchasing additional products or adding additional users would harm our future operating results.

In order for us to improve our operating results, it is important that our clients renew their agreements with us when the initial contract term expires and also purchase additional products or add additional users. Our clients have no obligation to renew their subscriptions after the initial subscription period, and we cannot assure you that our clients will renew their subscriptions at the same or a higher level of service, if at all. Every year, some of our clients elect not to renew their agreements with us. Moreover, certain of our clients have the right to cancel their agreements for convenience, subject to certain notice requirements and, in some cases, early termination fees. Our client renewal rates may decline or fluctuate as a result of a number of factors, including their satisfaction or dissatisfaction with our products, our pricing, the prices of competing products or services, mergers and acquisitions affecting our client base, reduced hiring by our clients or reductions in our clients' spending levels. If our clients do not renew their subscriptions, renew on less favorable terms, fail to purchase additional products or fail to add new users, our revenue

may decline and our operating results may be harmed.

Integrated, comprehensive SaaS products such as ours represent a relatively recent approach to addressing organizations' human capital management challenges, and we may be forced to change the prices we charge for our products, or the pricing model upon which they are based, as the market for these types of products evolves.

Providing organizations with applications to address their human capital management challenges through integrated, comprehensive SaaS products is a developing market. The market for these products is therefore still evolving, and competitive dynamics may cause pricing levels, as well as pricing models generally, to change, as the market matures and as existing and new market participants introduce new types of products and different approaches to enable organizations to address their human capital management needs. As a result, we may be forced to reduce the prices we charge for our products or the pricing model on which they are based, and may be unable to renew existing client agreements or enter into new client agreements at the same prices and upon the same terms that we have historically, which could have a material adverse effect on our revenue, gross margin and other operating results.

Evolving regulation of the Internet, changes in the infrastructure underlying the Internet, or interruptions in Internet access may adversely affect our financial condition by increasing our expenditures and causing client dissatisfaction.

As Internet commerce continues to evolve, regulation by federal, state or foreign agencies may increase. We are particularly sensitive to these risks because the Internet is a critical component of our business model. In addition, taxation of services provided over the Internet or other charges for accessing the Internet may be imposed by government agencies or private organizations. Changes in laws or regulations that adversely affect the growth, popularity or use of the Internet, or impact the way that Internet service providers treat Internet traffic, including laws impacting net neutrality, may negatively increase our operating costs or otherwise impact our business. Any regulation imposing greater fees for Internet use or restricting information exchanged over the Internet could result in a decline in the use of the Internet and the viability of Internet-based services, which could harm our business.

In addition, the rapid and continual growth of traffic on the Internet has resulted at times in slow connection and download speeds among Internet users. Our business expansion may be harmed if the Internet infrastructure cannot handle our clients' demands or if hosting capacity becomes insufficient. If our clients become frustrated with the speed at which they can utilize our products over the Internet, our clients may discontinue the use of our human capital management platform and choose not to renew their contracts with us. Further, the performance of the Internet has also been adversely affected by viruses, worms, hacking, phishing attacks, denial of service attacks and other similar malicious programs, as well as other forms of damage to portions of its infrastructure, which have resulted in a variety of Internet outages, interruptions and other delays. These service interruptions could diminish the overall attractiveness of our products to existing and potential users and could cause demand for our products to suffer.

We currently have a number of international offices and are expanding our international operations. Additionally, we do not have substantial experience in all international markets and may not achieve the results that we expect.

We currently have international offices in several countries, and we may expand our international operations into other countries in the future. International operations involve a variety of risks that may decrease demand for, or restrict our ability to sell or provide, our products, including:

- unexpected changes in regulatory requirements, taxes, trade laws, tariffs, export quotas, custom duties or other trade restrictions;
- differing labor regulations;
- regulations relating to data security and the unauthorized use of, or access to, commercial and personal information;
- potential penalties or other adverse consequences for violations of anti-corruption, anti-bribery and other similar laws and regulations, including the U.S. Foreign Corrupt Practices Act and the U.K. Bribery Act;
- greater difficulty in supporting and localizing our products;
- unrest and/or changes in a specific country's or region's social, political, legal or economic conditions;
- challenges inherent in efficiently managing an increased number of employees over large geographic distances, including the need to implement appropriate systems, controls, policies, benefits and compliance programs;
- currency exchange rate fluctuations, including any fluctuations caused by uncertainties relating to Brexit;
- limited or unfavorable intellectual property protection; and
- restrictions on repatriation of earnings.

We have less significant experience in marketing, selling and supporting our products and services abroad than domestically. Our less significant experience in operating our business internationally increases the risk that any potential future expansion efforts that we may undertake will not be successful. In addition, it may take us longer to build our presence in

international markets. If we invest substantial time and resources to expand our international operations and are unable to do so successfully and in a timely manner, our business and operating results will suffer.

Our operations could be materially affected by changes in domestic and foreign economic, political or legal conditions. For example, we are monitoring developments related to Brexit, which could have significant implications for our business. The political and economic instability created by the United Kingdom's vote to leave the EU has caused and may continue to cause significant volatility in global financial markets and the value of the British Pound currency or other currencies, including the Euro. Depending on the terms reached regarding any exit from the EU, it is possible that there may be adverse practical and/or operational implications on our business.

Failure to comply with anti-bribery, anti-corruption and anti-money laundering laws could subject us to penalties and other adverse consequences.

We are subject to the Foreign Corrupt Practices Act, or FCPA, the U.K. Bribery Act and other anti-corruption, anti-bribery and anti-money laundering laws in various jurisdictions both domestic and abroad. We leverage third parties, including channel partners, to sell subscriptions to our platform and conduct our business abroad. We and our third-party intermediaries may have direct or indirect interactions with officials and employees of government agencies or state-owned or affiliated entities and may be held liable for the corrupt or other illegal activities of these third-party business partners and intermediaries, our employees, representatives, contractors, channel partners and agents, even if we do not explicitly authorize such activities. While we have policies and procedure to address compliance with such laws, we cannot assure you that all of our employees and agents will not take actions in violation of our policies and applicable law, for which we may be ultimately held responsible. Any violation of the FCPA or other applicable anti-bribery, anti-corruption laws and anti-money laundering laws could result in whistleblower complaints, adverse media coverage, investigations, loss of export privileges, severe criminal or civil sanctions, or suspension or debarment from U.S. government contracts, all of which may have an adverse effect on our reputation, business, operating results and prospects.

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

We believe that developing and maintaining awareness of the Cornerstone OnDemand brand in a cost-effective manner is critical to achieving widespread acceptance of our existing and future products and is an important element in attracting new clients. Furthermore, we believe that the importance of brand recognition will increase as competition in our market increases. Successful promotion of our brand will depend largely on the effectiveness of our marketing efforts and on our ability to provide reliable and useful services at competitive prices. In the past, our efforts to build our brand have involved significant expenses. Brand promotion activities may not yield increased revenue, and even if they do, any increased revenue may not offset the expenses we incurred in building our brand. In addition, the Cornerstone OnDemand Foundation shares our company name and any negative perceptions of any kind about the Cornerstone OnDemand Foundation could adversely affect our brand and reputation. If we fail to successfully promote and maintain our brand, or incur substantial expenses in an unsuccessful attempt to promote and maintain our brand, we may fail to attract enough new clients or retain our existing clients to the extent necessary to realize a sufficient return on our brand-building efforts, and our business could suffer.

Our sales to government entities are subject to a number of additional challenges and risks.

We sell to U.S. federal and state and foreign governmental agency customers, and we may increase sales to government entities in the future. For example, in June 2017, we entered into an agreement with the U.S. Postal Service that authorizes, but does not guarantee, the purchase by the U.S. Postal Service of our software and services to support their more than 600,000 employees. The additional risks and challenges associated with doing business with governmental entities include, but are not limited to, the following:

- Selling to governmental entities can be more competitive, expensive and time-consuming than selling to private entities, often requiring significant upfront time and expense without any assurance that these efforts will generate a sale;
- Government certification requirements may change, or we may lose one or more government certifications, such as FedRAMP, and in doing so restrict our ability to sell into the government sector until we have attained revised certificates;
-

Governmental entities may have significant leverage in negotiations, thereby enabling such entities to demand contract terms that differ from what we generally agree to in our standard agreements, including, for example, most favored nation clauses and terms allowing contract termination for convenience;

- Government demand and payment for our products may be influenced by public sector budgetary cycles and funding authorizations, with funding reductions or delays having an adverse impact on public sector demand for our products; and

- Government contracts are generally subject to audits and investigations, which we have limited experience with, potentially resulting in termination of contracts, refund of a portion of fees received, forfeiture of profits, suspension of payments, fines and suspensions or debarment from future government business.

To the extent that we become more reliant on contracts with government entities in the future, our exposure to such risks and challenges could increase, which, in turn, could adversely impact our business.

If for any reason we are not able to develop enhancements and new features, keep pace with technological developments or respond to future disruptive technologies, our business will be harmed.

Our future success will depend on our ability to adapt and innovate. To attract new clients and increase revenue from existing clients, we will need to enhance and improve our existing products and introduce new features. The success of any enhancement or new feature depends on several factors, including timely completion, introduction and market acceptance. If we are unable to enhance our existing products to meet client needs or successfully develop or acquire new features or products, or if such new features or products fail to be successful, our business and operating results will be adversely affected.

In addition, because our products are designed to operate on a variety of network, hardware and software platforms using Internet tools and protocols, we will need to continuously modify and enhance our products to keep pace with changes in internet-related hardware, software, communication, browser and database technologies. If we are unable to respond in a timely and cost-effective manner to these rapid technological developments, our products may become less marketable and less competitive or obsolete, and our operating results may be negatively impacted.

Finally, our ability to grow is subject to the risk of future disruptive technologies. If new technologies emerge that are able to deliver a human capital management platform at lower prices, more efficiently or more conveniently, such technologies could adversely impact our ability to compete.

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

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

Further, the indenture governing the convertible notes due 2021 includes a restrictive covenant that, subject to specified exceptions and parameters, limits our ability to incur additional debt. We may be unable to take advantage of strategic or business development opportunities as they arise, or we may not be able to react to market conditions, if we are restricted in our ability to raise debt financing, or we may be required to seek alternative means to generate cash, including by selling assets, refinancing or obtaining additional equity capital on terms that may be onerous or highly dilutive, if available at all.

In addition, in connection with the sale of our convertible notes due 2012, we entered into an investment agreement with Silver Lake providing Silver Lake with the option to purchase all or a portion of any equity securities, or instruments convertible into or exchangeable for any equity securities, in any proposed offerings by us until the earlier of June 2019 or such time as Silver Lake no longer has a representative and no longer has rights to have a representative on our Board. Although Silver Lake’s option will not apply to equity securities issued in connection with acquisitions, underwritten public offerings, strategic partnerships or commercial arrangements, or equity compensation plans, Silver Lake’s participation rights could impact our ability to raise additional capital.

Servicing our debt will require a significant amount of cash, which could adversely affect our business, financial condition and results of operations.

Our ability to make scheduled payments of the principal of, to pay interest on or to refinance our indebtedness, including our convertible notes due 2021 and 2018, which represent an aggregate principal amount of $553.0 million, depends on our future performance, which is subject to economic, financial, competitive and other factors beyond our control. Our business may not generate cash flow from operations in the future sufficient to satisfy our obligations under the notes and any future

indebtedness we may incur and to make necessary capital expenditures. If we are unable to generate such cash flow, we may be required to adopt one or more alternatives, such as reducing or delaying investments or capital expenditures, selling assets, refinancing or obtaining additional equity capital on terms that may be onerous or highly dilutive. Our ability to refinance the notes or future indebtedness will depend on the capital markets and our financial condition at such time. We may not be able to engage in any of these activities or engage in these activities on desirable terms, which could result in a default on the notes or future indebtedness.

Further, with certain exceptions, upon a change of control, the holders of our convertible notes due 2021 may require that we repurchase all or part of such notes at a purchase price equal to the principal amount plus the total sum of all remaining scheduled interest payments through the remainder of the term of the notes. In addition, with certain exceptions, upon a change of control, the holders of our convertible notes due 2018 may require us to purchase all or a portion of such notes for cash at a price equal to the principal amount of such notes plus any accrued and unpaid interest to, but excluding, the effective date of the change of control. In such event, we may not have enough cash available or be able to obtain financing to repurchase the notes, and our ability to repurchase notes may be limited by law, regulatory authority or agreements governing our other indebtedness.

Because of how we recognize revenue, a significant downturn in our business may not be immediately reflected in our operating results.

Generally, we recognize revenue from subscription agreements monthly over the terms of these agreements, which is typically three years for our human capital management platform. As a result, a significant portion of the revenue we report in each quarter is generated from client agreements entered into during previous periods. Consequently, a decline in new subscriptions in any one quarter may not significantly impact our revenue and financial performance in that quarter, but will negatively affect our revenue, or rate of revenue growth and financial performance in future quarters.

In addition, if subscription agreements expire and are not renewed in the same quarter, our revenue and financial performance in that quarter and subsequent quarters will be negatively affected. However, the revenue impact may not be immediately reflected in our operating results to the extent there is an offsetting increase in revenue from services contracts performed in that same quarter.

Finally, we may be unable to adjust our fixed costs in response to reduced revenue. Accordingly, the effect of significant declines in sales and market acceptance of our products may not be reflected in our short-term operating results.

Because we generally recognize subscription revenue from our clients over the terms of their agreements but incur most costs associated with generating such agreements upfront, rapid growth in our client base may put downward pressure on our operating income in the short term.

The expenses associated with generating client agreements are generally incurred up front but the resulting subscription revenue is generally recognized over the life of the agreements; therefore, increased growth in the number of our clients will result in our recognition of more costs than revenue during the early periods covered by such agreements, even in cases where the agreements are expected to be profitable for us over their full terms.

We have a history of losses, and we cannot be certain that we will achieve or sustain profitability.

We have incurred losses since our inception. We experienced net losses of $16.2 million, $61.3 million, $66.8 million and $85.5 million for the three months ended March 31, 2018, and years ended December 31, 2017, 2016 and 2015, respectively. At March 31, 2018, our accumulated deficit was $512.3 million and total stockholders' equity was $32.4 million. We expect to continue to incur operating losses as a result of expenses associated with the continued development and expansion of our business. Our expenses include among others, sales and marketing, research and development, consulting and support services and other costs relating to the development, marketing and sale and service of our products that may not generate revenue until later periods, if at all. Any failure to increase revenue or manage our cost structure as we implement initiatives to grow our business could prevent us from achieving or sustaining profitability. In addition, our ability to achieve profitability is subject to a number of the risks and uncertainties discussed below, many of which are beyond our control. We cannot be certain that we will be able to achieve or sustain profitability on a quarterly or annual basis.

The conversion feature of the convertible notes due 2018 could adversely affect our financial condition and operating results.

In the event the conditional conversion feature of the convertible notes due 2018 is triggered, holders of such notes will be entitled to convert the notes at any time during specified periods at their option. In addition, holders of these notes may convert all or a portion of their notes at any time on and after April 1, 2018. If one or more holders elect to convert their notes, we would be required to settle a portion of our conversion obligation through the payment of cash, which could adversely

affect our liquidity. In addition, even if holders do not elect to convert their notes, we could be required under applicable accounting rules to reclassify all or a portion of the outstanding principal of the notes as a current rather than long-term liability, which would result in a material reduction of our net working capital.

The accounting methods for our convertible debt securities may have a material effect on our reported financial results.

In May 2008, the Financial Accounting Standards Board, or FASB, issued FASB Staff Position No. APB 14-1, Accounting for Convertible Debt Instruments That May Be Settled in Cash Upon Conversion (Including Partial Cash Settlement), which has subsequently been codified as Accounting Standards Codification 470-20, Debt with Conversion and Other Options, which we refer to as ASC 470-20. Under ASC 470-20, an entity must separately account for the liability and equity components of the convertible debt instruments (such as the convertible notes due 2018) that may be settled entirely or partially in cash upon conversion in a manner that reflects the issuer's economic interest cost. The effect of ASC 470-20 on the accounting for the convertible notes due 2018 is that the equity component is required to be included in the additional paid-in capital section of stockholders' equity on our consolidated balance sheet, and the value of the equity component would be treated as original issue discount for purposes of accounting for the debt component of the notes. As a result, we will be required to record a greater amount of non-cash interest expense in current periods presented as a result of the amortization of the discounted carrying value of the convertible notes due 2018 to their face amount over the term of the notes. We will report lower net income (or greater net loss) in our financial results because ASC 470-20 will require interest to include both the current period's amortization of the debt discount and the instrument's coupon interest, which could adversely affect our reported or future financial results, the market price of our common stock and the trading price of the notes.

In addition, convertible debt instruments (such as the convertible notes due 2018) that may be settled entirely or partly in cash are currently accounted for utilizing the treasury stock method, the effect of which is that the shares issuable upon conversion of the notes are not included in the calculation of diluted earnings per share except to the extent that the conversion value of the notes exceeds their principal amount. Under the treasury stock method, for diluted earnings per share purposes, the transaction is accounted for as if the number of shares of common stock that would be necessary to settle such excess, if we elected to settle such excess in shares, are issued. We cannot be sure that the accounting standards in the future will continue to permit the use of the treasury stock method. In contrast, our convertible notes due 2021 may be settled upon conversion only in shares of our common stock. As a result, the shares issuable upon conversion of these notes will be included in the calculation of diluted earnings per share assuming the conversion of the notes at the beginning of the reporting period if the impact is dilutive. To the extent that we are required to include shares issuable upon conversion of our convertible debt securities in the calculation of diluted earnings per share, our diluted earnings per share will be adversely affected.

The nature of our business requires the application of complex revenue and expense recognition rules and the current legislative and regulatory environment affecting GAAP is uncertain. Changes in financial accounting standards or practices may cause adverse, unexpected financial reporting fluctuations and affect our reported operating results.

The accounting rules and regulations that we must comply with are complex and subject to interpretation by the FASB, the SEC and various bodies formed to promulgate and interpret appropriate accounting principles. In addition, many companies’ accounting disclosures are being subjected to heightened scrutiny by regulators and the public. A change in accounting standards or practices can have a significant effect on our reported results and may even affect our reporting of transactions completed before the change is effective. New accounting pronouncements and varying interpretations of accounting pronouncements have occurred and may occur in the future. Changes to existing rules or the questioning of current practices may adversely affect our reported financial results or the way we conduct our business.

For example, in May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes nearly all existing revenue recognition guidance under GAAP. We adopted Topic 606 on the effective date of January 1, 2018, using the modified retrospective transition method, and plan to implement changes to our accounting, internal controls and disclosures to support the new standard. Under this guidance, revenue is recognized when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods and services. The guidance is expected to

impact the timing and recognition of costs to obtain contracts with customers, such as commissions, and may result in variability in our revenue recognition from period to period that may cause unexpected variability in our operating results. Any difficulties in implementing this new standard could cause us to fail to meet our financial reporting obligations, which could result in regulatory discipline, harm investors' confidence in us, and adversely affect our stock price.

To the extent that our pre-tax income or loss becomes relatively modest, our ability to conclude that a control deficiency is not a material weakness or that an accounting error does not require a restatement could be adversely affected.

Under the Sarbanes-Oxley Act of 2002, our management is required to assess the impact of control deficiencies based upon both quantitative and qualitative factors, and depending upon that analysis, we classify such identified deficiencies as either a control deficiency, significant deficiency or a material weakness. One element of our analysis of the significance of any control deficiency is its actual or potential financial impact. This assessment will vary depending on our level of pre-tax income or loss. For example, a smaller pre-tax income or loss will increase the likelihood of a quantitative assessment of a control deficiency as a significant deficiency or material weakness.

To the extent that our pre-tax income or loss is relatively small, if management or our independent registered public accountants identify an error in our interim or annual financial statements, it is more likely that such an error may be determined to be a material weakness or be considered a material error that could, depending upon the complete quantitative and qualitative analysis, result in our having to restate previously issued financial statements.

If we fail to adequately protect our proprietary rights, our competitive advantage and brand could be impaired and we may lose valuable assets, generate reduced revenue and incur costly litigation to protect our rights.

Our success is dependent, in part, upon protecting our proprietary technology. We rely on a combination of patents, copyrights, trademarks, service marks, trade secret laws and contractual restrictions to establish and protect our proprietary rights in our products and services. However, the steps we take to protect our intellectual property may be inadequate. We will not be able to protect our intellectual property if we are unable to enforce our rights or if we do not detect unauthorized use of our intellectual property. Despite our precautions, it may be possible for unauthorized third parties to copy our products and use information that we regard as proprietary to create products and services that compete with ours. Some license provisions protecting against unauthorized use, copying, transfer and disclosure of our licensed products may be unenforceable under the laws of certain jurisdictions and foreign countries. Further, the laws of some countries do not protect proprietary rights to the same extent as the laws of the United States. To the extent we expand our international activities, our exposure to unauthorized copying and use of our products and proprietary information may increase. We enter into confidentiality and invention assignment agreements with our employees and consultants and enter into confidentiality agreements with the parties with whom we have strategic relationships and business alliances. These agreements may not be effective in controlling access to and distribution of our products and proprietary information. Further, these agreements do not prevent our competitors from independently developing technologies that are substantially equivalent or superior to our products. Litigation brought to protect and enforce our intellectual property rights could be costly, time consuming and distracting to management and could result in the impairment or loss of portions of our intellectual property. If we fail to secure, protect and enforce our intellectual property rights, we may lose valuable assets, generate reduced revenue and incur costly litigation to protect our rights, which could seriously harm our brand and adversely impact our business.

We may be sued by third parties for alleged infringement of their proprietary rights or may find it necessary to enter into licensing arrangements with third parties to settle or forestall such claims, either of which could have a material adverse effect on our operating results and financial condition.

There is considerable patent and other intellectual property development activity in our industry. Our success depends in part upon our not infringing the intellectual property rights of others. However, our competitors, as well as a number of other entities and individuals, may own or claim to own intellectual property relating to our industry or, in some cases, our technology or products. From time to time, such third parties may claim that we are infringing their intellectual property rights, and we may actually be found to be infringing such rights. Moreover, we may be subject to claims of infringement with respect to technology that we acquire or license from third parties. The risk that we could be subject to infringement claims is increasing as the number of products and companies competing with our platform grows. Any claims or litigation could require the commitment of substantial time and resources and, if successfully asserted against us, could require that we pay substantial damages or ongoing royalty or licensing payments, indemnify our clients, distributors or other third parties, modify or discontinue the sale of our products, or refund fees, any of which would deplete our resources and adversely impact our business. We have in the past obtained, and may in the future obtain, licenses from third parties to forestall or settle potential claims that our

products and technology infringe the intellectual property rights of others. Discussions and negotiations with such third parties, whether successful or unsuccessful, could result in substantial costs and the diversion of management resources, either of which could seriously harm our business.

Indemnity provisions in various agreements potentially expose us to substantial liability for intellectual property infringement and other losses.

Our agreements with clients and other third parties may include indemnification provisions under which we agree to indemnify them for losses suffered or incurred as a result of claims of intellectual property infringement, damages caused by us to property or persons, or other liabilities relating to or arising from our products, services or other contractual obligations. The term of these indemnity provisions generally survives termination or expiration of the applicable agreement. Large indemnity payments could harm our business, operating results and financial condition. From time to time, we are requested by clients to indemnify them for breach of confidentiality with respect to personal data. Although we normally do not agree to, or contractually limit our liability with respect to, such requests, the existence of such a dispute with a client may have adverse effects on our client relationships and reputation.

We use open source software in our products, which could subject us to litigation or other actions.

We use open source software in our products and may use more open source software in the future. From time to time, there have been claims challenging the ownership of open source software against companies that incorporate open source software into their products. As a result, we could be subject to suits by parties claiming ownership of what we believe to be open source software. Litigation could be costly for us to defend, have a negative effect on our operating results and financial condition or require us to devote additional research and development resources to change our products. In addition, if we were to combine our proprietary software products with open source software in a certain manner, we could, under certain of the open source licenses, be required to release the source code of our proprietary software products. If we inappropriately use open source software, we may be required to re-engineer our products, discontinue the sale of our products or take other remedial actions.

We are subject to governmental export and import controls that could impair our ability to compete in international markets due to licensing requirements and subject us to liability if we are not in full compliance with applicable laws.

Our products are subject to export controls, including the Commerce Department’s Export Administration Regulations and various economic and trade sanctions regulations established by the Treasury Department’s Office of Foreign Assets Controls, and exports of our products must be made in compliance with these laws. If we fail to comply with these U.S. export control laws and import laws, including U.S. Customs regulations, we and certain of our employees could be subject to substantial civil or criminal penalties, including the possible loss of export or import privileges; fines, which may be imposed on us and responsible employees or managers; and, in extreme cases, the incarceration of responsible employees or managers. In addition, if our distributors fail to obtain appropriate import, export or re-export licenses or authorizations, we may also be adversely affected through reputational harm and penalties. Obtaining the necessary authorizations, including any required license, for a particular sale may be time-consuming and is not guaranteed, and may result in the delay or loss of sales opportunities. Furthermore, the U.S. export control laws and economic sanctions laws prohibit the shipment of certain products and services to U.S. embargoed or sanctioned countries, governments and persons. Even though we take precautions to prevent our products from being shipped or provided to U.S. sanctions targets, our products and services could be shipped to those targets or provided by our distributors despite such precautions. Any such shipment could have negative consequences, including government investigations, penalties and reputational harm. In addition, various countries regulate the import of certain encryption technology, including through import permitting or licensing requirements, and have enacted laws that could limit our ability to distribute our products or could limit our clients’ ability to implement our products in those countries. Changes to our products or changes in export and import regulations may create delays in the introduction and sale of our products in international markets, prevent our clients with international operations from deploying our products or, in some cases, prevent the export or import of our products to certain countries, governments or persons altogether. Any change in export or import regulations, economic sanctions or related laws, shift in the enforcement or scope of existing regulations, or change in the countries, governments, persons or technologies targeted by such regulations, could result in decreased use of our products, or in our decreased ability to export or sell our products to existing or potential clients with international operations. Any decreased use of our products or limitation on our ability to export or sell our products would likely adversely affect our business, financial condition and operating results.

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We rely on implementation partners to deliver professional services to our clients, and if these implementation partners fail to deliver these professional services effectively, or if we are unable to incentivize new partners to service our customers, our operating results will be harmed.

We rely on various partners to assist us in the successful implementation of our products and to optimize our clients' use of our products during the terms of their engagements. We provide our implementation partners with specific training and programs to assist them in servicing our clients, but there can be no assurance that these steps will be utilized or effective. If these partners fail to deliver these services to our customers in an effective and timely manner, we may suffer reputational harm and our results of operations may be adversely impacted. We also may not be able to incentivize new partners to service our customers. If we are unable to maintain our existing relationships or enter into new ones, we would have to devote substantially more resources to delivering our professional services. If we fail to effectively manage our implementation partners, our ability to sell our products and subscriptions and our operating results will be harmed.

Our investment portfolio is subject to general credit, liquidity, counterparty, market and interest rate risks, any of which could impair the market value of our investments and harm our financial results.

At March 31, 2018, we had $413.3 million in cash and cash equivalents and $222.9 million in short-term and long-term investments in marketable securities, consisting of corporate bonds, money market funds backed by United States Treasury Bills, U.S. treasury securities and agency securities. Although we follow an established investment policy and set of guidelines to manage our investment portfolio, our investments are subject to general credit, liquidity, counterparty, market and interest rate risks, which have been exacerbated by the recent financial and credit crisis, rising bankruptcy filings in the United States and the ongoing debt-ceiling debate.

Because the market value of fixed-rate debt securities may be adversely impacted by a rise in interest rates, our future investment income may fall short of expectations if interest rates rise. In addition, we may suffer losses if we are forced to sell securities that have experienced a decline in market value because of changes in interest rates. Currently, we do not use financial derivatives to hedge our interest rate exposure.

The fair value of our investments may change significantly due to events and conditions in the credit and capital markets. Any investment securities that we hold, or the issuers of such securities, could be subject to review for possible downgrade. Any downgrade in these credit ratings may result in an additional decline in the estimated fair value of our investments. Changes in the various assumptions used to value these securities and any increase in the perceived market risk associated with such investments may also result in a decline in estimated fair value.

In the event of adverse conditions in the credit and capital markets, and to the extent we make future investments, our investment portfolio may be impacted, and we could determine that some or all of our investments experienced an other-than-temporary decline in fair value, requiring impairment, which could adversely impact our financial position and operating results.

We may invest in companies for strategic reasons and may not realize a return on our investments.

In November 2013, we launched a strategic initiative created to invest in, advise and collaborate with promising cloud startups building innovative business applications that support the continued expansion of our market reach. We have made, and from time to time may continue to make, strategic investments in privately-held companies. The privately-held companies in which we may invest are considered inherently risky. The technologies and products these companies have under development are typically in the early stages and may never materialize, which could result in a loss of all or a substantial part of our initial investment in these companies. The evaluation of privately-held companies is based on information that we request from these companies, which is not subject to the same disclosure regulations as U.S. publicly traded companies, and as such, the basis for these evaluations is subject to the timing and accuracy of the data received from these companies.

Risks Related to Tax Issues

We are a multinational organization faced with increasingly complex tax issues in many jurisdictions, and we could be obligated to pay additional taxes in various jurisdictions.

As a multinational organization, we are subject to taxation in several jurisdictions around the world with increasingly complex tax laws, the application of which can be uncertain. The amount of taxes we pay in these jurisdictions could increase substantially as a result of changes in the applicable tax principles, including increased tax rates, new tax

laws or revised interpretations of existing tax laws and precedents, which could have a material adverse effect on our liquidity and operating results. In addition, the authorities in these jurisdictions could review our tax returns and impose additional tax, interest and penalties, and the authorities could claim that various withholding requirements apply to us or our subsidiaries or assert that benefits of tax treaties are not available to us or our subsidiaries, any of which could have a material impact on us and our

operating results. If we are selected for future examinations that uncover incorrect tax positions, we could be subject to additional taxes, interest and penalties.

Taxing authorities could reallocate our taxable income among our subsidiaries, which could increase our consolidated tax liability.

We conduct operations worldwide through subsidiaries in various tax jurisdictions pursuant to transfer pricing arrangements between our subsidiaries. If two or more affiliated companies are located in different countries, the tax laws or regulations of each country generally will require that transfer prices be the same as those between unrelated companies dealing at arms' length and that contemporaneous documentation is maintained to support the transfer prices. While we believe that we operate in compliance with applicable transfer pricing laws and intend to continue to do so, our transfer pricing procedures are not binding on applicable tax authorities. If tax authorities in any of these countries were to successfully challenge our transfer prices as not reflecting arm's length transactions, they could require us to adjust our transfer prices and thereby reallocate our income to reflect these revised transfer prices, which could result in a higher tax liability to us. In addition, if the country from which the income is reallocated does not agree with the reallocation, both countries could tax the same income, resulting in double taxation. If tax authorities were to allocate income to a higher tax jurisdiction, subject our income to double taxation or assess interest and penalties, it would increase our consolidated tax liability, which could adversely affect our financial condition, operating results and cash flows.

The recently passed comprehensive tax reform bill could adversely affect our business and financial condition.

On December 22, 2017, new legislation was enacted that significantly revises the Internal Revenue Code of 1986, as amended. The newly enacted federal income tax law, among other things, contains significant changes to corporate taxation, including reduction of the corporate tax rate from a top marginal rate of 35% to a flat rate of 21%, limitation of the tax deduction for interest expense to 30% of adjusted earnings (except for certain small businesses), limitations on the deductibility of executive compensation, limitation of the deduction for net operating losses to 80% of current year taxable income and elimination of net operating loss carrybacks, one time taxation of offshore earnings at reduced rates regardless of whether they are repatriated, elimination of U.S. tax on foreign earnings (subject to certain important exceptions), immediate deductions for certain new investments instead of deductions for depreciation expense over time, and modifying or repealing many business deductions and credits. Notwithstanding the reduction in the corporate income tax rate, the overall impact of the new federal tax law is uncertain and our business and financial condition could be adversely affected. In addition, it is uncertain if and to what extent various states will conform to the newly enacted federal tax law. The Act's new international rules, including the Global Intangible Low-Taxed Income, the Foreign Derived Intangible Income and the Base Erosion Anti-Avoidance Tax, are highly complex and may affect our financial condition as additional interpretive guidance is issued. The impact of this tax reform on holders of our common stock is also uncertain and could be adverse. We urge our stockholders to consult with their legal and tax advisors with respect to this legislation and the potential tax consequences of investing in or holding our common stock.

Our ability to use net operating loss carryforwards to reduce future tax payments may be subject to limitations.

We have federal and state net operating loss carryforwards that will begin to expire, if not utilized. These net operating loss carryforwards could expire unused and be unavailable to offset future income tax liabilities. Under the newly enacted federal income tax law, federal net operating losses incurred in 2018 and in future years may be carried forward indefinitely, but the deductibility of such federal net operating losses may be limited. It is uncertain if and to what extent various states will conform to the newly enacted federal tax law. In addition, under Section 382 of the Internal Revenue Code of 1986, as amended, if a corporation undergoes an "ownership change" (generally defined as a greater than 50% change (by value) in its equity ownership over a three year period), the corporation's ability to use its pre-change net operating loss carryforwards and other pre-change tax attributes (such as research tax credits) to offset its post-change income may be limited. We may experience ownership changes in the future and subsequent shifts in our stock ownership. As a result, we may be limited in the portion of net operating loss carryforwards that we can use in the future to offset taxable income for U.S. Federal income tax purposes.

Risks Related to Ownership of Our Common Stock

The trading price of our common stock may be volatile.

The trading price of our common stock has at times been volatile and could continue to be subject to significant fluctuations in response to various factors, some of which are beyond our control. In addition, the stock market in general, and the market for technology companies in particular, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of the companies operating in such markets. The market price of our common stock may be similarly volatile, and investors in our common stock may experience a decrease in the value of their shares, including as a result of factors unrelated to our operating performance and prospects. The market price of our common stock could be subject to wide fluctuations in response to a number of factors, including:

- our operating performance and the performance of other similar companies;
- the financial or non-financial metric projections we provide to the public, including the failure of the projections to meet the expectations of securities analysts or investors, and any changes in these projections or our failure to meet or exceed these projections;
- the overall performance of the equity markets;
- developments with respect to intellectual property rights;
- publication of unfavorable research reports about us or our industry or withdrawal of research coverage by securities analysts;
- speculation in the press or investment community;
- the size of our public float;
- natural disasters or terrorist acts;
- data breach;
- announcements by us or our competitors of significant contracts, new technologies, acquisitions, commercial relationships, joint ventures or capital commitments; and
- global economic, legal and regulatory factors unrelated to our performance.

In addition, in the past, following periods of volatility in the overall market and the market price of a particular company's securities, securities class action litigation has often been initiated against these companies. This litigation, if initiated against us, could result in substantial costs and a diversion of our management's attention and resources.

If securities or industry analysts do not publish research or publish misleading or unfavorable research about our business, the market price of our common stock and trading volume could decline.

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

The issuance of additional stock in connection with acquisitions, our stock incentive plans or otherwise will dilute all other stockholdings.

Our certificate of incorporation authorizes us to issue up to 1,000,000,000 shares of common stock and up to 50,000,000 shares of preferred stock with such rights and preferences as may be determined by our board of directors. Subject to compliance with applicable rules and regulations, we may issue all of these shares that are not already outstanding without any action or approval by our stockholders. We intend to continue to evaluate strategic acquisitions in the future. We may pay for such acquisitions, partly or in full, through the issuance of additional equity. Any issuance of shares in connection with our acquisitions, the exercise of stock options, the vesting of restricted stock units or otherwise would dilute the percentage ownership held by existing investors.

We cannot guarantee that our recently announced share repurchase program will be fully consummated or that it will enhance shareholder value, and share repurchases could affect the trading price of our common stock.

In November 2017, our board of directors authorized a $100.0 million share repurchase program. Although our board of directors has authorized the share repurchase program, the share repurchase program does not obligate us to repurchase any specific dollar amount or to acquire any specific number of shares. The share repurchase program could affect the price of our common stock, increase volatility and diminish our cash reserves. In addition, it may be suspended or terminated at any time, which may result in a decrease in the price of our common stock.

Conversion of our convertible notes may dilute the ownership interest of existing stockholders, including holders who had previously converted their notes, or may otherwise depress the price of our common stock.

The conversion of some or all of our convertible notes due 2021 and the conversion of all or some of our convertible notes due 2018, to the extent we deliver shares upon conversion of the 2018 notes, will dilute the ownership interests of existing stockholders. Any sales in the public market of our common stock issuable upon such conversion could adversely affect prevailing market prices of our common stock. In addition, the existence of the notes may encourage short selling by market participants because the conversion of the notes could be used to satisfy short positions, or anticipated conversion of the notes into shares of our common stock could depress the price of our common stock.

We do not expect to declare any dividends in the foreseeable future.

We do not anticipate declaring any cash dividends to holders of our common stock in the foreseeable future. Consequently, investors may need to sell all or part of their holdings of our common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investment. Investors seeking cash dividends should not purchase our common stock.

Anti-takeover provisions in our charter documents and Delaware law may delay or prevent an acquisition of our company.

Our certificate of incorporation, our bylaws and Delaware law contain provisions that may have the effect of delaying or preventing a change in control of us or changes in our management. Our certificate of incorporation and our bylaws include provisions that:

- authorize “blank check” preferred stock, which could be issued by the board without stockholder approval and may contain voting, liquidation, dividend and other rights superior to our common stock;
- create a classified board of directors whose members serve staggered three-year terms;
- specify that special meetings of our stockholders can be called only by our board of directors, the chairperson of the board, the chief executive officer or the president;
- establish an advance notice procedure for stockholder approvals to be brought before an annual meeting of our stockholders, including proposed nominations of persons for election to our board of directors;
- provide that our directors may be removed only for cause;
- provide that vacancies on our board of directors may be filled only by a majority of directors then in office, even though less than a quorum;
- specify that no stockholder is permitted to cumulate votes at any election of directors; and
- require supermajority votes of the holders of our common stock to amend specified provisions of our charter documents.

These provisions, alone or together, could delay or prevent hostile takeovers and changes in control or changes in our management.

In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which limits the ability of stockholders owning in excess of 15% of our outstanding voting stock to merge or combine with us.

Any provision of our certificate of incorporation, our bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.

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

Not applicable.

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ITEM 3. Defaults Upon Senior Securities
Not applicable.

ITEM 4. Mine Safety Disclosures
Not applicable.

ITEM 5. Other Information
Not applicable.

ITEM 6. Exhibits

| Exhibit Number | Exhibit Description | Incorporated by Reference | | | |
|---|---|---|---|---|---|
| | | Form | File No. | Exhibit | Filing Date |
| 10.1* | Employment Agreement between the Registrant and Adrianna Burrows, dated February 13, 2018. | | | | |
| 10.2* | Transition Agreement between the Registrant and David J. Carter, dated as of February 27, 2018. | 10-K | 001-35098 | 10.2 | February 27, 2018 |
| 10.3* | Transition Agreement between the Registrant and Kirsten Helvey, dated as of February 27, 2018. | 10-K | 001-35098 | 10.3 | February 27, 2018 |
| 10.4* | Investment Agreement, dated as of November 8, 2017, by and between, inter alia, the Registrant and Silver Lake Credit Partners, L.P., as amended | 10-K | 001-35098 | 10.4 | February 27, 2018 |
| 10.5* | Description of 2018 Executive Bonus Plan | 8-K | 001-35098 | n/a | February 27, 2018 |
| 31.1 | Certification of the Chief Executive Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002. | | | | |
| 31.2 | Certification of the Chief Financial Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002. | | | | |
| 32.1† | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002. | | | | |
| 32.2† | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted 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 or arrangement

† The certifications attached as Exhibit 32.1 and 32.2 that accompany this Quarterly Report on Form 10-Q are not deemed filed with the Securities and Exchange Commission and are not to be incorporated by reference into any filing of Cornerstone OnDemand, Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

†† The financial information contained in these XBRL documents is unaudited.

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SIGNATURE

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

Cornerstone OnDemand, Inc.
(Registrant)

/s/ Brian L. Swartz
Brian L. Swartz
Chief Financial Officer
(Duly Authorized Officer and Principal Financial and Accounting Officer)
Date: May 8, 2018