

LIVEPERSON INC
Form 10-Q
August 06, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 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: 000-30141

LIVEPERSON, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware 13-3861628

(State or Other Jurisdiction of
Incorporation or Organization) (IRS Employer Identification No.)

475 Tenth Avenue, 5th Floor 10018
New York, New York

(Address of Principal Executive Offices) (Zip Code)

(212) 609-4200

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 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, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one).

Large accelerated filer ý Accelerated filer ¨

Non-accelerated filer ¨ Smaller reporting company ¨

(Do not check if a 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. ¨

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

On July 27, 2018, 62,408,378 shares of the registrant's common stock were outstanding.

LIVEPERSON, INC.
 June 30, 2018
 FORM 10-Q
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FORWARD-LOOKING STATEMENTS

STATEMENTS IN THIS REPORT ABOUT LIVEPERSON, INC. THAT ARE NOT HISTORICAL FACTS ARE FORWARD-LOOKING STATEMENTS BASED ON OUR CURRENT EXPECTATIONS, ASSUMPTIONS, ESTIMATES AND PROJECTIONS ABOUT LIVEPERSON AND OUR INDUSTRY. THESE FORWARD-LOOKING STATEMENTS ARE SUBJECT TO RISKS AND UNCERTAINTIES THAT COULD CAUSE ACTUAL FUTURE EVENTS OR RESULTS TO DIFFER MATERIALLY FROM SUCH STATEMENTS. ANY SUCH FORWARD-LOOKING STATEMENTS ARE MADE PURSUANT TO THE SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995. IT IS ROUTINE FOR OUR INTERNAL PROJECTIONS AND EXPECTATIONS TO CHANGE AS THE YEAR OR EACH QUARTER IN THE YEAR PROGRESSES, AND THEREFORE IT SHOULD BE CLEARLY UNDERSTOOD THAT THE INTERNAL PROJECTIONS AND BELIEFS UPON WHICH WE BASE OUR EXPECTATIONS MAY CHANGE PRIOR TO THE END OF EACH QUARTER OR THE YEAR. ALTHOUGH THESE EXPECTATIONS MAY CHANGE, WE ARE UNDER NO OBLIGATION TO INFORM YOU IF THEY DO. OUR COMPANY POLICY IS GENERALLY TO PROVIDE OUR EXPECTATIONS ONLY ONCE PER QUARTER, AND NOT TO UPDATE THAT INFORMATION UNTIL THE NEXT QUARTER. ACTUAL EVENTS OR RESULTS MAY DIFFER MATERIALLY FROM THOSE CONTAINED IN THE PROJECTIONS OR FORWARD-LOOKING STATEMENTS. FACTORS THAT COULD CAUSE OR CONTRIBUTE TO SUCH DIFFERENCES INCLUDE THOSE DISCUSSED IN PART II, ITEM 1A, "RISK FACTORS."

Part I. Financial Information

Item 1. Financial Statements

LIVEPERSON, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS)

(UNAUDITED)

	June 30, 2018	December 31, 2017 (Note 1)
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$69,747	\$ 56,115
Cash held as collateral	216	1,451
Accounts receivable, net of allowance for doubtful accounts of \$1,672 and \$1,318 as of June 30, 2018 and December 31, 2017, respectively	38,109	37,926
Prepaid expenses and other current assets	16,885	7,352
Total current assets	124,957	102,844
Property and equipment, net	38,066	34,705
Intangibles, net	12,321	12,366
Goodwill	80,473	80,531
Deferred tax assets	817	753
Other assets	1,787	1,600
Total assets	\$258,421	\$ 232,799
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$6,207	\$ 5,481
Accrued expenses and other current liabilities	39,252	48,011
Deferred revenue	47,375	35,563
Total current liabilities	92,834	89,055
Deferred revenue	2,131	—
Other liabilities	2,584	2,766
Deferred tax liability	1,020	915
Total liabilities	98,569	92,736
Commitments and contingencies		
STOCKHOLDERS' EQUITY:		
Common stock	62	60
Additional paid-in capital	337,238	305,676
Treasury stock	(3) (3
Accumulated deficit	(173,983) (163,135
Accumulated other comprehensive loss	(3,462) (2,535
Total stockholders' equity	159,852	140,063
Total liabilities and stockholders' equity	\$258,421	\$ 232,799

See Notes to Condensed Consolidated Financial Statements (unaudited).

LIVEPERSON, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
 (UNAUDITED)

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2018	2017	2018	2017
Revenue	\$ 61,660	\$ 54,074	\$ 119,901	\$ 104,993
Costs and expenses ^{(1) (2)}				
Cost of revenue ⁽³⁾	16,036	15,134	29,990	28,915
Sales and marketing	25,392	23,392	49,523	45,092
General and administrative	11,499	10,437	21,622	20,130
Product development	14,219	9,326	27,471	19,285
Restructuring costs	1,906	2,076	2,084	2,315
Amortization of purchased intangibles	424	470	848	942
Total costs and expenses	69,476	60,835	131,538	116,679
Loss from operations	(7,816)	(6,761)	(11,637)	(11,686)
Other income (expense), net	31	(99)	160	221
Loss before provision for income taxes	(7,785)	(6,860)	(11,477)	(11,465)
Provision for income taxes	536	673	47	1,744
Net loss	\$ (8,321)	\$ (7,533)	\$ (11,524)	\$ (13,209)
Net loss per share of common stock:				
Basic	\$ (0.14)	\$ (0.13)	\$ (0.20)	\$ (0.24)
Diluted	\$ (0.14)	\$ (0.13)	\$ (0.20)	\$ (0.24)
Weighted-average shares used to compute net loss per share:				
Basic	58,648,195	55,954,158	57,982,648	55,964,568
Diluted	58,648,195	55,954,158	57,982,648	55,964,568

⁽¹⁾ Amounts include stock-based compensation expense, as follows:

Cost of revenue	\$ 230	\$ 117	\$ 384	\$ 193
Sales and marketing	1,373	754	2,259	1,408
General and administrative	1,182	774	2,022	1,436
Product development	1,041	702	1,599	1,223

⁽²⁾ Amounts include depreciation expense, as follows:

Cost of revenue	\$ 1,931	\$ 1,870	\$ 3,847	\$ 3,635
Sales and marketing	371	408	727	789
General and administrative	274	340	520	590
Product development	852	427	1,692	824

⁽³⁾ Amounts include amortization of purchased intangibles, as follows:

Cost of revenue	\$ 287	\$ 959	\$ 574	\$ 1,918
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See Notes to Condensed Consolidated Financial Statements (unaudited).

LIVEPERSON, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
 (IN THOUSANDS)
 (UNAUDITED)

	Three Months Ended		Six months ended	
	June 30,		June 30,	
	2018	2017	2018	2017
Net loss	\$ (8,321)	\$ (7,533)	\$ (11,524)	\$ (13,209)
Foreign currency translation adjustment	1,486	(1,220)	927	(4,618)
Comprehensive loss	\$ (6,835)	\$ (8,753)	\$ (10,597)	\$ (17,827)

See Notes to Condensed Consolidated Financial Statements (unaudited).

LIVEPERSON, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	Six Months Ended June 30,	
	2018	2017
OPERATING ACTIVITIES:		
Net loss	\$(11,524)	\$(13,209)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Stock-based compensation expense	6,264	4,260
Depreciation	6,786	5,838
Amortization of purchased intangibles	1,422	2,860
Amortization of tenant allowance	(83)	(83)
Deferred income taxes	41	(13)
Provision for doubtful accounts, net	862	958
Changes in operating assets and liabilities:		
Accounts receivable	(1,045)	6,011
Prepaid expenses and other current assets	(9,531)	(3,864)
Other assets	(187)	(31)
Accounts payable	34	(3,881)
Accrued expenses and other current liabilities	(8,771)	(3,204)
Deferred revenue	13,943	9,477
Other liabilities	(218)	245
Net cash (used in) provided by operating activities	(2,007)	5,364
INVESTING ACTIVITIES:		
Purchases of property and equipment, including capitalized software	(9,664)	(7,011)
Cash held as collateral for foreign exchange forward contracts	1,235	205
Payments for acquisitions and intangible assets, net of cash acquired	(392)	(239)
Net cash used in investing activities	(8,821)	(7,045)
FINANCING ACTIVITIES:		
Proceeds from issuance of common stock in connection with the exercise of options	25,667	2,588
Repurchase of common stock	(1,345)	(1,781)
Net cash provided by financing activities	24,322	807
EFFECT OF FOREIGN EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	138	4,350
CHANGE IN CASH AND CASH EQUIVALENTS	13,632	3,476
CASH AND CASH EQUIVALENTS - Beginning of the period	56,115	50,889
CASH AND CASH EQUIVALENTS - End of the period	\$69,747	\$54,365
SUPPLEMENTAL DISCLOSURE OF OTHER CASH FLOW INFORMATION:		
Cash paid for income taxes	\$5,553	\$659
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Purchase of property and equipment recorded in accounts payable	\$774	\$41

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Issuance of 85,861 shares of common stock in connection with the BotCentral transaction on January 24, 2018	\$1,000	\$—
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See Notes to Condensed Consolidated Financial Statements (unaudited).

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LIVEPERSON, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. Description of Business and Basis of Presentation

LivePerson, Inc. (the “Company” or “LivePerson”) was incorporated in the State of Delaware in November 1995 and the LivePerson service was introduced in November 1998. In April 2000, the Company completed an initial public offering and is currently traded on the NASDAQ Global Select Market and the Tel Aviv Stock Exchange. LivePerson is headquartered in New York City with U.S. offices in Alpharetta (Georgia), Mountain View (California) and Seattle (Washington), and international offices in Amsterdam (Netherlands), Berlin (Germany), London (United Kingdom), Mannheim (Germany), Melbourne (Australia), Milan (Italy), Paris (France), Ra'anana (Israel), Reading (United Kingdom), Tel Aviv (Israel), and Tokyo (Japan).

LivePerson provides mobile and online business messaging solutions that power digital communication between brands and consumers. LiveEngage, the Company’s enterprise-class, cloud-based platform, enables businesses and consumers to connect through conversational interfaces, such as in-app and mobile messaging, while leveraging bots and artificial intelligence (AI) to increase efficiency. As consumers have reoriented their digital lives around the smartphone, messaging apps have become their preferred communication channel to connect with each other.

LivePerson allows brands to align with this new consumer preference, and deploy messaging at scale for customer care, marketing, and sales, instead of requiring that consumers use email or call a 1-800 number.

LiveEngage was designed to securely deploy messaging, coupled with bots and AI, at scale for brands with tens of millions of customers and many thousands of customer care agents. LiveEngage powers conversations across each of a brand’s primary digital channels, including mobile apps, mobile and desktop web browsers, short message services (SMS), social media and third-party consumer messaging platforms. Brands can also use LiveEngage to message consumers when they dial a 1-800 number instead of having them navigate interactive voice response systems (IVR) and wait on hold. The platform seamlessly integrates with third-party bots, enabling brands to manage both AI- based agents and human agents from a single console.

LivePerson optimizes campaign outcomes for sales and service transactions by combining website visitor data with other historical, behavioral, and operational information to develop insights into each step of a consumer’s journey.

LivePerson’s products, coupled with its domain knowledge, industry expertise and consulting services, have been proven to maximize the effectiveness of consumer engagement.

The Company’s primary revenue source is from the sale of LivePerson services to businesses of all sizes. The Company also offers an online marketplace that connects independent service providers (“Experts”) who provide information and knowledge for a fee via real-time chat with individual consumers (“Users”).

Basis of Presentation

The accompanying condensed consolidated financial statements as of June 30, 2018 and for the three and six months ended June 30, 2018 and 2017 are unaudited. In the opinion of management, the unaudited condensed consolidated financial statements have been prepared on the same basis as the annual financial statements and reflect all adjustments, which include only normal recurring adjustments, necessary to present fairly the consolidated financial position of LivePerson as of June 30, 2018, and the consolidated results of operations, comprehensive loss and cash flows for the interim periods ended June 30, 2018 and 2017. The financial data and other information disclosed in these notes to the condensed consolidated financial statements related to these periods are unaudited. The results of operations for any interim period are not necessarily indicative of the results of operations for any other future interim period or for a full fiscal year. The condensed consolidated balance sheet at December 31, 2017 has been derived from audited consolidated financial statements at that date.

Certain information and note disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States (“GAAP”) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). These unaudited interim condensed consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements and notes thereto for the year ended December 31, 2017 included in the Company’s Annual Report on Form 10-K filed with the SEC on March 15, 2018.

Principles of Consolidation

The condensed consolidated financial statements include the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated.

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Use of Estimates

The preparation of the Company's condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of income and expenses during the reporting period. These estimates are based on information available as of the date of the condensed consolidated financial statements; therefore, actual results could differ from management's estimates.

Recently Issued Accounting Standards

In June 2018, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No.2018-07 "Compensation —Stock Compensation (Topic 718) —Improvements to Nonemployee Share-Based Payment Accounting" ("ASU 2018-07"). This new standard expands the scope of Topic 718, Compensation—Stock Compensation (which currently only includes share-based payments to employees) to include share-based payments issued to non-employees for goods or services. Consequently, the accounting for share-based payments to non-employees and employees will be substantially aligned. ASU 2018-05 is effective for public companies for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. The Company is currently evaluating the impact of this updated standard, but does not believe this update will have a significant impact on its consolidated financial statements.

In March 2018, the FASB issued ASU No.2018-05 "Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118" ("ASU 2018-05"). This new standard adds SEC paragraphs pursuant to the SEC Staff Accounting Bulletin No. 118, which expresses the view of the staff regarding application of Topic 740, Income Taxes, in the reporting period that includes December 22, 2017 - the date on which the Tax Cuts and Jobs Act (H.R.1, An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018) was signed into law. ASU 2018-05 is effective upon inclusion in the FASB Codification. The Company is currently evaluating the impact of this updated standard, but does not believe this update will have a significant impact on its consolidated financial statements.

In February 2018, the FASB issued ASU No. 2018-02 "Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income" ("ASU 2018-02"). This new standard allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017. The amendments in ASU 2018-02 affects any entity that is required to apply the provisions of Topic 220 and has items of other comprehensive income for which the related tax effects are presented in other comprehensive income as required by GAAP. The Company is currently evaluating the impact of this updated standard, but does not believe this update will have a significant impact on its consolidated financial statements.

In August 2017, the FASB issued ASU No. 2017-12 "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities" ("ASU 2017-12"). This new standard refines and expands hedge accounting for both financial (e.g., interest rate) and commodity risks. Its provisions create more transparency around how economic results are presented, both on the face of the financial statements and in the footnotes, for investors and analysts. ASU 2017-12 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, for public companies. Early adoption is permitted in any interim period or fiscal years before the effective date of the standard. The Company does not expect the adoption of ASU 2017-12 to have a material effect on its financial position, results of operations or cash flows.

In January 2017, FASB issued ASU No. 2017-04, "Intangibles —Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment" ("ASU 2017-04"). This update addresses concerns over the cost and complexity of the two-step goodwill impairment test. The amendments in this update remove the second step of the test. An entity will apply a one-step quantitative test and record the amount of goodwill impairment as the excess of a reporting unit's carrying amount over its fair value, not to exceed the total amount of goodwill allocated to the reporting unit. The new guidance does not amend the optional qualitative assessment of goodwill impairment. ASU 2017-04 is effective for financial statements issued for annual periods beginning after December 15, 2019, and interim periods within those annual periods. The Company does not expect the adoption of ASU 2017-04 to have a material effect on its financial

position, results of operations or cash flows.

In February 2016, the FASB issued ASU No. 2016-02, "Leases" ("ASU 2016-02"). ASU 2016-02 requires lessees to recognize the following for all leases (with the exception of short-term leases) at the commencement date: a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, "Revenue from Contracts with Customers". The new lease guidance also simplified the accounting for sale and leaseback transactions primarily because lessees must recognize lease assets and lease liabilities. Lessees will no longer be provided with a source of off-balance sheet financing. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest

comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. ASU 2016-02 is effective for financial statements issued for annual periods beginning after December 15, 2018. The Company is currently assessing the provisions of this guidance and evaluating the timing and impact the guidance will have on its consolidated financial statements and related disclosures. The Company is also in the process of aggregating lease documentation for review. The adoption of this ASU primarily impacts the balance sheet through the recognition of a right-of-use asset and a lease liability for all leases with terms in excess of twelve months. This guidance is effective January 1, 2019 using a modified retrospective transition approach with early adoption permitted.

Recently Adopted Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers" ("Topic 606"). Topic 606 supersedes the revenue recognition requirements in Accounting Standards Codification ("ASC") Topic 605, "Revenue Recognition" ("Topic 605"), and requires the recognition of revenue when promised goods or services are transferred to customers in an amount that reflects the considerations to which the entity expects to be entitled to 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. Collectively, the Company refers to Topic 606 and Subtopic 340-40 as the "new standard."

The Company adopted the requirements of the new standard as of January 1, 2018, utilizing the modified retrospective method applied to those contracts which were not completed as of January 1, 2018. Results for the reporting periods beginning after January 1, 2018 are presented under the new standard, while prior period amounts are not adjusted and continue to be reported in accordance with its historic accounting under Topic 605.

The impact of adopting the new standard as of January 1, 2018 on revenues was not material. The primary impact of adopting the new standard relates to the deferral of incremental commission costs of obtaining subscription contracts. The Company recorded an addition to opening retained earnings of \$0.7 million as of January 1, 2018 due to the impact of adopting the new standard, with the impact related to the deferral of incremental commission costs. Under Topic 605, the Company deferred only direct and incremental commission costs to obtain a contract and amortized those costs on a straight-line basis over the term of the related subscription contract, which was generally one year. Under the new standard, the Company defers all incremental commission costs to obtain the contract. The prepaid commission balance as of June 30, 2018 is \$7.9 million. The Company amortizes these costs over the related period of benefit using the customer expected life that the Company determined to be three to five years which is consistent with the transfer to the customer of the services to which the asset relates.

2. Revenue Recognition

The majority of the Company's revenue is generated from monthly service revenues and related professional services from the sale of the LivePerson services. Revenues are recognized when control of these services is transferred to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for those services.

The Company determines revenue recognition through the following steps:

- Identification of the contract, or contracts, with a customer;
- Identification of the performance obligations in the contract;
- Determination of the transaction price;
- Allocation of the transaction price to the performance obligations in the contract; and
- Recognition of revenue when, or as, the Company satisfies a performance obligation.

Total revenue of \$61.7 million and \$119.9 million recognized during the three months and six months ended June 30, 2018, under Topic 606, was not materially different from what would have been recognized under Topic 605.

Hosted Services- Business Revenue

Hosted Services Business revenue is reported at the amount that reflects the ultimate consideration expected to be received and primarily consist of fees that provide customers access to LiveEngage, the Company's enterprise-class,

cloud-based platform. The Company has determined such access represents a stand-ready service provided continually throughout the contract term. As such, control and satisfaction of this stand-ready performance obligation is deemed to occur over time. The Company recognizes this revenue over time on a ratable basis over the contract term, beginning on the date that access to the LiveEngage platform is made available to the customer. The passage of time is deemed to be the most faithful depiction of the transfer of control of the services as the customer simultaneously receives and consumes the benefit provided by the Company's performance. Subscription contracts are generally one year or longer in length, billed, monthly, quarterly or annually in advance. There is no significant

variable consideration related to these arrangements. Additionally, for certain of the Company's larger customers, the Company may provide call center labor through an arrangement with one or more of several qualified vendors. For most of these customers, the Company passes the fee it incurs with the labor provider and its fee for the hosted services through to its customers in the form of a fixed fee for each order placed via the Company's online engagement solutions. For these Pay for Performance ("PFP") arrangements in accordance with ASC-606, "Principal Agent Considerations", the Company acts as a principal in a transaction if it controls the specified goods or services before they are transferred to the customer.

Professional Services Revenues

Professional services revenue primarily consists of fees for deployment and optimization services, as well as training delivered on an on-demand basis which is deemed to represent a distinct stand-ready performance obligation. Professional Services Revenues are reported at the amount that reflects the ultimate consideration the Company expects to receive in exchange for such services. Control for the majority of the Company's Professional Services contracts passes over time to the customer and is recognized ratably over the contracted period, as the passage of time is deemed to be the most faithful depiction of the transfer of control. For certain deployment services, which are not deemed to represent a distinct performance obligation, revenue will be recognized in the same manner as the fee for access to the LiveEngage platform, and as such will be recognized on a straight-line basis over the contract term. For services billed on a fixed price basis, revenue is recognized over time based on the proportion performed using inputs as the measure of progress toward complete satisfaction of the performance obligation. Professional service contracts are generally one year or longer in length, billed, monthly, quarterly or annually in advance. There is no significant variable consideration related to these arrangements.

Contracts with Multiple Performance Obligations

Some of the Company's contracts with customers contain multiple performance obligations. For these contracts, the Company accounts for individual performance obligations separately if they are distinct. The transaction price is allocated to the separate performance obligations on a relative standalone selling price basis. The Company determines the standalone selling prices based on its overall pricing objectives, taking into consideration market conditions and other factors, including the value of its contracts, the cloud applications sold, and the number and types of users within its contracts.

Hosted Services- Consumer Revenue

For revenue from the Company's Consumer segment generated from online transactions between Experts and Users, revenue is recognized at an amount net of Expert fees in accordance with ASC 606, "Principal Agent Considerations," due primarily to the fact that the Expert is the primary obligor. Additionally, the Company performs as an agent without any risk of loss for collection, and is not involved in selecting the Expert or establishing the Expert's fee. The Company collects a fee from the consumer and retains a portion of the fee, and then remit the balance to the Expert. Revenue from these transactions is recognized at the point in time when the transaction is complete and no significant performance obligations remain.

Deferred Revenues

The Company records deferred revenues when cash payments are received or due in advance of its performance. The increase in the deferred revenue balance for the six months ended June 30, 2018 is primarily driven by cash payments received or due in advance of satisfying its performance obligations, partially offset by \$26.2 million of revenues recognized that were included in the deferred revenue balance as of December 31, 2017. The following table presents deferred revenue by revenue source (amounts in thousands):

	Deferred Revenue	
	As of	As of
	June 30,	December
	2018	31, 2017
Hosted services – Business	\$38,063	\$ 27,011
Hosted services – Consumer	—	—
Professional services	11,443	8,552
Total deferred revenue	\$49,506	\$ 35,563

Disaggregated Revenue

The following table presents the Company's revenues disaggregated by revenue source (amounts in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
Revenue:				
Hosted services – Business	\$48,331	\$43,927	\$95,759	\$85,420
Hosted services – Consumer	4,952	4,460	9,632	8,630
Professional services	8,377	5,687	14,510	10,943
Total revenue	\$61,660	\$54,074	\$119,901	\$104,993

(1) As noted above, prior period amounts have not been adjusted under the modified retrospective method.

Revenue by Geographic Location

The following table presents the Company's revenues attributable to domestic and foreign operations for the periods presented (amounts in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
United States	\$35,572	\$34,078	\$69,643	\$65,763
Other Americas ⁽¹⁾	2,547	1,968	3,806	3,940
Total Americas	38,119	36,046	73,449	69,703
EMEA ^{(2) (4)}	17,519	13,953	34,438	27,465
APAC ⁽³⁾	6,022	4,075	12,014	7,825
Total revenue	\$61,660	\$54,074	\$119,901	\$104,993

(1) Canada, Latin America and South America

(2) Europe, the Middle East and Africa (“EMEA”)

(3) Asia-Pacific (“APAC”)

(4) Includes revenues from the United Kingdom of \$11.9 million and \$9.1 million for the three months ended June 30, 2018 and 2017, respectively, and \$23.5 million and \$18.2 million six months ended June 30, 2018 and 2017, respectively.

Information about Contract Balances

Amounts collected in advance of services being provided are accounted for as deferred revenue. Nearly all of the Company's deferred revenue balance is related to Hosted Services- Business Revenue.

In some arrangements, the Company allows customers to pay for access to LiveEngage over the term of the software license. The Company refers to these as subscription transactions. Amounts recognized as revenue in excess of amounts billed are recorded as unbilled receivables. Unbilled receivables, anticipated to be invoiced in the next twelve months, are included in accounts receivable on the consolidated balance sheet. The opening and closing balances of the Company's accounts receivable, unbilled receivables, and deferred revenues are as follows (amounts in thousands):

Accounts Receivable	Unbilled Receivable	Deferred Revenue (current)	Deferred Revenue (long term)
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Opening Balance as of December 31, 2017	\$ 30,342	\$ 7,584	\$ 35,563	\$ —
Increase (decrease), net	(640) 823	11,812	2,131
Ending Balance as of June 30, 2018	\$ 29,702	\$ 8,407	\$ 47,375	\$ 2,131

As of June 30, 2018, the Company expects to recognize the long term performance obligations in 2019.

3. Net Loss Per Share

The Company calculates earnings per share (“EPS”) in accordance with the provisions of ASC 260-10 and the guidance of SEC Staff Accounting Bulletin (“SAB”) No. 98. Under ASC 260-10, basic EPS excludes dilution for common stock equivalents and is computed by dividing net income or loss attributable to common shareholders by the weighted average number of common shares outstanding for the period. All options, warrants or other potentially dilutive instruments issued for nominal consideration are required to be included in the calculation of basic and diluted net income attributable to common stockholders. Diluted EPS is calculated using the treasury stock method and reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock and resulted in the issuance of common stock.

Diluted net loss per common share for the three and six months ended June 30, 2018 does not include the effect of 9,784,690 outstanding common stock awards, as the effect of their inclusion is anti-dilutive. Diluted net loss per common share for the three and six months ended June 30, 2017 does not include the effect of 9,423,000 outstanding common stock awards, as the effect of their inclusion is anti-dilutive.

A reconciliation of shares used in calculating basic and diluted net loss per share follows:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2018	2017	2018	2017
Basic	58,648,195	55,954,158	57,982,648	55,964,568
Effect of assumed exercised options	—	—	—	—
Diluted	58,648,195	55,954,158	57,982,648	55,964,568

4. Segment Information

The Company accounts for its segment information in accordance with the provisions of ASC 280-10, “Segment Reporting.” ASC 280-10 establishes annual and interim reporting standards for operating segments of a company. ASC 280-10 requires disclosures of selected segment-related financial information about products, major customers, and geographic areas based on the Company’s internal accounting methods. The Company is organized into two operating segments for purposes of making operating decisions and assessing performance. The Business segment enables brands to leverage LiveEngage’s sophisticated intelligence engine to connect with consumers through an integrated suite of mobile and online business messaging technologies. The Consumer segment facilitates online transactions between independent service providers (“Experts”) and individual consumers (“Users”) seeking information and knowledge for a fee via mobile and online messaging. Both segments currently generate their revenue primarily in the United States. The chief operating decision maker, who is the chief executive officer, evaluates performance, makes operating decisions, and allocates resources based on the operating income of each segment. The reporting segments follow the same accounting policies used in the preparation of the Company’s condensed consolidated financial statements which are described in the summary of significant accounting policies. The Company allocates cost of revenue, sales and marketing and amortization of purchased intangibles to the segments, but it does not allocate product development expenses, general and administrative expenses, restructuring costs and income tax expense because management does not use this information to measure performance of the operating segments. There are currently no inter-segment sales.

Summarized financial information by segment for the three months ended June 30, 2018, based on the Company’s internal financial reporting system utilized by the Company’s chief operating decision maker, follows (amounts in thousands):

	Business	Consumer	Corporate	Consolidated
Revenue:				
Hosted services – Business	\$ 48,331	\$ —	\$ —	\$ 48,331
Hosted services – Consumer	—	4,952	—	4,952
Professional services	8,377	—	—	8,377
Total revenue	56,708	4,952	—	61,660
Cost of revenue	15,086	950	—	16,036

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Sales and marketing	23,339	2,053	—	25,392
Amortization of purchased intangibles	424	—	—	424
Unallocated corporate expenses	—	—	27,624	27,624
Operating income (loss)	\$ 17,859	\$ 1,949	\$(27,624)	\$(7,816)

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Summarized financial information by segment for the three months ended June 30, 2017, based on the Company's internal financial reporting system utilized by the Company's chief operating decision maker, follows (amounts in thousands):

	Business	Consumer	Corporate	Consolidated
Revenue:				
Hosted services – Business	\$43,927	\$ —	\$—	\$ 43,927
Hosted services – Consumer	—	4,460	—	4,460
Professional services	5,687	—	—	5,687
Total revenue	49,614	4,460	—	54,074
Cost of revenue	14,206	928	—	15,134
Sales and marketing	21,242	2,150	—	23,392
Amortization of purchased intangibles	470	—	—	470
Unallocated corporate expenses	—	—	21,839	21,839
Operating income (loss)	\$ 13,696	\$ 1,382	\$(21,839)	\$ (6,761)

Summarized financial information by segment for the six months ended June 30, 2018, based on the Company's internal financial reporting system utilized by the Company's chief operating decision maker, follows (amounts in thousands):

	Business	Consumer	Corporate	Consolidated
Revenue:				
Hosted services – Business	\$95,759	\$ —	\$—	\$ 95,759
Hosted services – Consumer	—	9,632	—	9,632
Professional services	14,510	—	—	14,510
Total revenue	110,269	9,632	—	119,901
Cost of revenue	28,004	1,986	—	29,990
Sales and marketing	45,062	4,461	—	49,523
Amortization of purchased intangibles	848	—	—	848
Unallocated corporate expenses	—	—	51,177	51,177
Operating income (loss)	\$ 36,355	\$ 3,185	\$(51,177)	\$ (11,637)

Summarized financial information by segment for the six months ended June 30, 2017, based on the Company's internal financial reporting system utilized by the Company's chief operating decision maker, follows (amounts in thousands):

	Business	Consumer	Corporate	Consolidated
Revenue:				
Hosted services – Business	\$85,420	\$ —	\$—	\$ 85,420
Hosted services – Consumer	—	8,630	—	8,630
Professional services	10,943	—	—	10,943
Total revenue	96,363	8,630	—	104,993
Cost of revenue	27,112	1,803	—	28,915
Sales and marketing	40,785	4,307	—	45,092
Amortization of purchased intangibles	942	—	—	942
Unallocated corporate expenses	—	—	41,730	41,730
Operating income (loss)	\$ 27,524	\$ 2,520	\$(41,730)	\$ (11,686)

Geographic Information

The Company is domiciled in the United States and has international operations in the Israel, United Kingdom, Asia-Pacific, Latin America and Western Europe, particularly France and Germany. The following table presents the Company's long-lived assets by geographic region as of the dates presented (amounts in thousands):

	June 30, 2018	December 31, 2017
United States	\$99,307	\$95,716
Israel	13,597	13,079
Australia	9,134	9,504
Netherlands	7,992	8,363
Other ⁽¹⁾	3,434	3,293
Total long-lived assets	\$133,464	\$129,955

⁽¹⁾ United Kingdom, Germany, Japan, France and Italy

No individual customer accounted for 10% or more of consolidated revenue for any of the periods presented. No individual customer accounted for 10% or more of accounts receivable as of June 30, 2018 and December 31, 2017.

5. Goodwill and Intangible Assets

Goodwill

The changes in the carrying amount of goodwill for the six months ended June 30, 2018 are as follows (amounts in thousands):

	Business	Consumer	Consolidated
Balance as of December 31, 2017	\$72,507	\$ 8,024	\$ 80,531
Adjustments to goodwill:			
Foreign exchange adjustment	(58)	—	(58)
Balance as of June 30, 2018	\$72,449	\$ 8,024	\$ 80,473

Intangible Assets

Intangible assets are summarized as follows (amounts in thousands):

	As of June 30, 2018			Weighted
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Average Amortization Period
Amortizing intangible assets:				
Technology	\$29,040	\$ (22,879)	\$ 6,161	5.3 years
Customer relationships	15,973	(11,110)	4,863	8.0 years
Trade names	1,287	(1,287)	—	2.1 years
Non-compete agreements	1,437	(1,437)	—	2.3 years
Patents	1,832	(562)	1,270	13.3 years
Other	262	(235)	27	2.7 years
Total	\$49,831	\$ (37,510)	\$ 12,321	

As of December 31, 2017

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Amortization Period
Amortizing intangible assets:				
Technology	\$27,882	\$ (22,197)	\$ 5,685	5.3 years
Customer relationships	15,978	(10,457)	5,521	8.0 years
Trade names	1,289	(1,283)	6	2.1 years
Non-compete agreements	1,439	(1,439)	—	2.3 years
Patents	1,620	(493)	1,127	13.1 years
Other	262	(235)	27	2.7 years
Total	\$48,470	\$ (36,104)	\$ 12,366	

Amortization expense is calculated over the estimated useful life of the asset. Aggregate amortization expense for intangible assets was \$0.7 million and \$1.4 million for the three months ended June 30, 2018 and 2017, respectively, and \$1.4 million and \$2.9 million for the six months ended June 30, 2018 and 2017, respectively. For the three and six months ended June 30, 2018 and 2017, respectively, a portion of this amortization is included in cost of revenue.

Estimated amortization expense for the next five years is as follows (amounts in thousands):

	Estimated Amortization Expense
2018	\$ 1,422
2019	2,641
2020	2,452
2021	2,240
2022	1,893
Thereafter	1,673
Total	\$ 12,321

BotCentral

In January 2018, the Company acquired the employees and technology assets of BotCentral, a Silicon Valley based startup, for an approximate purchase price of \$1.0 million in common stock of the Company. The Company incurred an additional \$0.2 million related to acquisition costs. This transaction was accounted for as an asset purchase. The aggregate amount of approximately \$1.2 million is included in "Intangibles, net" on the Company's June 30, 2018 condensed consolidated balance sheet. While an active participant in the LiveEngage for Bots partner program, the BotCentral team created a number of bot solutions for major brands in banking, insurance, and travel, running on LivePerson's conversational platform. With the team's expertise and knowledge of the LiveEngage platform, the team is bringing valuable insight for LivePerson's customers and partners, and enabling the company to more rapidly optimize its bot deployment capabilities, and grow the ecosystem.

6. Property and Equipment

The following table presents the detail of property and equipment for the periods presented (amounts in thousands):

	June 30, 2018	December 31, 2017
Computer equipment and software	\$109,885	\$ 100,392
Furniture, equipment and building improvements	13,691	13,546
	123,576	113,938
Less: accumulated depreciation	(85,510)	(79,233)
Total	\$38,066	\$ 34,705

7. Accrued Expenses and Other Current Liabilities

The following table presents the detail of accrued expenses and other current liabilities for the periods presented (amounts in thousands):

	June 30, December 31,	
	2018	2017
Payroll and other employee related costs	\$13,357	\$ 16,431
Professional services and consulting and other vendor fees	16,318	15,674
Unrecognized tax benefits	2,277	4,924
Sales commissions	4,147	5,259
Restructuring (see Note 11)	2,577	2,338
Other	576	3,385
Total	\$39,252	\$ 48,011

8. Fair Value Measurements

The Company measures its cash equivalents at fair value based on an expected exit price as defined by the authoritative guidance on fair value measurements, which represents the amount that would be received on the sale of an asset or paid to transfer a liability, as the case may be, in an orderly transaction between market participants. As such, fair value may be based on assumptions that market participants would use in pricing an asset or liability. The authoritative guidance on fair value measurements establishes a consistent framework for measuring fair value on either a recurring or nonrecurring basis whereby inputs, used in valuation techniques, are assigned a hierarchical level. The following are the hierarchical levels of inputs to measure fair value:

Level 1: Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2: Inputs reflect: quoted prices for identical assets or liabilities in markets that are not active; quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the assets or liabilities; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3: Unobservable inputs reflecting the Company's assumptions incorporated in valuation techniques used to determine fair value. These assumptions are required to be consistent with market participant assumptions that are reasonably available.

Financial Assets and Liabilities

The carrying amount of cash, accounts receivable, and accounts payable approximate their fair value due to their short-term nature. The Company's assets and liabilities that are measured at fair value on a recurring basis, by level, within the fair value hierarchy as of June 30, 2018 and December 31, 2017, are summarized as follows (amounts in thousands). The Company's restricted cash balance of \$0.2 million at June 30, 2018 and \$1.5 million at December 31, 2017 is not held in a money market account and is not included in the following table.

	June 30, 2018				December 31, 2017			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets:								
Cash equivalents:								
Money market funds	\$2,817	\$ —	\$ —	\$ —	\$2,806	\$ —	\$ —	\$ —
Foreign currency derivative contracts	—	—	—	—	—	65	—	65
Total assets	\$2,817	\$ —	\$ —	\$ —	\$2,806	\$ 65	\$ —	\$ —
Liabilities:								
Foreign currency derivative contracts	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 2	\$ —	\$ —
Total liabilities	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 2	\$ —	\$ —

In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible as well as considers counterparty credit risk in its

assessment of

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fair value. Observable or market inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's assumptions based on the best information available.

The Company's money market funds are measured at fair value on a recurring basis based on quoted market prices in active markets and are classified as level 1 within the fair value hierarchy. On a nonrecurring basis, the Company uses fair value measures when analyzing asset impairment. Long-lived tangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If it is determined such indicators are present and the review indicates that the assets will not be fully recoverable, based on undiscounted estimated cash flows over the remaining amortization periods, their carrying values are reduced to estimated fair value. The Company uses an income approach and inputs that constitute level 3. During the third quarter of each year, the Company evaluates goodwill for impairment at the reporting unit level. The Company uses qualitative factors in accordance with ASU No. 2011-08 to determine whether it is "more likely than not" that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. This measurement is classified based on level 3 input.

Derivative Financial Instruments

The Company is exposed to foreign exchange risks that in part are managed by using derivative financial instruments. The Company entered into foreign currency forward contracts related to risks associated with foreign operations. The Company does not use derivatives for trading purposes. Derivatives are recorded at their estimated fair values based upon Level 2 inputs. Derivatives designated and effective as cash flow hedges are reported as a component of other comprehensive income and reclassified to earnings in the same periods in which the hedged transactions impact earnings. Gains and losses related to derivatives not meeting the requirements of hedge accounting and the portion of derivatives related to hedge ineffectiveness are recognized in current earnings.

In accordance with the foreign currency forward contracts, the Company was required to pledge cash as collateral security to be maintained at the bank. The collateral shall remain in control of the lender, and these funds can be used to satisfy the outstanding obligation. Accordingly, the Company had cash at the bank of approximately \$0.2 million at June 30, 2018 and \$1.5 million at December 31, 2017, which is recorded as cash held as collateral in current assets. The following summarizes certain information regarding the Company's outstanding foreign currency derivative contracts related primarily to intercompany receivables and payables for the periods presented (in thousands):

	As of June 30, 2018	As of December 31, 2017
Notional amount of foreign currency derivative contracts	\$	—\$ 2,866
Fair value of foreign currency derivatives contracts	\$	—\$ 63

The fair value of the Company's derivative instruments is summarized below (in thousands):

	Balance Sheet Location	Fair Value of Derivative Instruments As of June 30, 2018	As of December 31, 2017
Derivative Assets			
Derivatives not designated as hedging instruments:			
Foreign currency derivatives contracts	Prepaid expenses and other current assets	\$	—\$ 65
Derivative Liabilities			
Derivatives not designated as hedging instruments:			
Foreign currency derivatives contracts	Accrued expenses and other liabilities	\$	—\$ 2

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The following summarizes certain information regarding the Company's derivatives that are not designated or are not effective as hedges (in thousands):

		Gain (losses) on Derivative Instruments Recognized in Statements of Operations		
		Three Months Ended June 30, 2017	Six Months Ended June 30, 2018	2017
Foreign currency derivatives contracts	Other (income) expense	\$ -38	\$(50)	\$213

9. Commitments and Contingencies

Contractual Obligations

The Company leases facilities and certain equipment under agreements accounted for as operating leases. These leases generally require the Company to pay all executory costs such as maintenance and insurance. Rental expense for operating leases for the three months ended June 30, 2018 and 2017 was approximately \$2.3 million. Rental expense for operating leases for the six months ended June 30, 2018 and 2017 was approximately \$4.6 million.

Employee Benefit Plans

The Company has a 401(k) defined contribution plan covering all eligible employees. The Company provides for employer matching contributions equal to 50% of employee contributions, up to the lesser of 5% of eligible compensation or \$6,000. Matching contributions are deposited into the employee's 401(k) account and are subject to 5 year graded vesting. Salaries and related expenses include \$0.4 million of employer matching contributions for both the three months ended June 30, 2018 and 2017. Salaries and related expenses include \$0.9 million and \$0.8 million of employer matching contributions for the six months ended June 30, 2018 and 2017, respectively.

Letters of Credit

As of June 30, 2018, the Company has a \$1.9 million letter of credit outstanding substantially in favor of a certain landlord for office space. In addition, the Company has a letter of credit totaling \$0.1 million as a security deposit for the due performance by the Company of the terms and conditions of a supply contract. There were no draws against these letters of credit during the six months ended June 30, 2018.

10. Stockholders' Equity

Common Stock

As of June 30, 2018, there were 100,000,000 shares of common stock authorized, and 62,366,602 shares issued and outstanding. As of December 31, 2017, there were 100,000,000 shares of common stock authorized, and 59,663,969 shares issued and outstanding. The par value for common shares is \$0.001.

Preferred Stock

As of June 30, 2018 and December 31, 2017, there were 5,000,000 shares of preferred stock authorized, and zero shares issued and outstanding. The par value for preferred shares is \$0.001.

Stock Repurchase Program

On December 10, 2012, the Company's Board of Directors approved a stock repurchase program through June 30, 2014. Under the stock repurchase program, the Company is authorized to repurchase shares of its common stock, in the open market or privately negotiated transactions, at times and prices considered appropriate by the Board of Directors depending upon prevailing market conditions and other corporate considerations. On March 13, 2014, the Company's Board of Directors increased the aggregate purchase price of the stock repurchase program from \$30.0 million to \$40.0 million. On July 23, 2014, the Company's Board of Directors increased the aggregate purchase price of the stock repurchase program from \$40.0 million to \$50.0 million. On February 16, 2016, the Company's Board of Directors increased the aggregate purchase price of the total stock repurchase program by an additional \$14.0 million. On November 21, 2016, the Company's Board of Directors increased the aggregate purchase price of the stock repurchase program from \$64.0 million to \$74.0 million and extended the expiration date of the program out to December 31, 2017. On May 7, 2018, the Company's Board of Directors ratified the extension to December 31, 2018 of the repurchase program, effective as of January 1, 2018. There were 93,750 shares repurchased under this program during the six months ended June 30, 2018, which were recorded in treasury stock at par on the condensed consolidated balance sheets as of June 30, 2018. As of June 30, 2018, approximately \$17.1 million remained available for purchase under the program.

Stock-Based Compensation

The Company follows FASB ASC 718-10, "Stock Compensation," which addresses the accounting for transactions in which an entity exchanges its equity instruments for goods or services, with a primary focus on transactions in which an entity obtains employee services in share-based payment transactions. ASC 718-10 requires measurement of the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award (with limited exceptions). Incremental compensation costs arising from subsequent modifications of awards after the grant date must be recognized.

The per share weighted average fair value of stock options granted was \$8.15 and \$3.55 during the three months ended June 30, 2018 and 2017, respectively, and \$6.26 and \$3.50 during the six months ended June 30, 2018 and 2017, respectively. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
Dividend yield	0.0%	0.0%	0.0%	0.0%
Risk-free interest rate	2.6% - 2.8%	1.7% - 1.9%	2.5% - 2.8%	1.7% - 1.9%
Expected life (in years)	5	5	5	5
Historical volatility	43.7% - 48.4%	46.6% - 47.6%	43.7% - 48.4%	46.6% - 47.6%

A description of the methods used in the significant assumptions used to estimate the fair value of stock-based compensation awards follows:

Dividend yield – The Company uses 0% as it has never issued dividends and does not anticipate issuing dividends in the near term.

Risk-free interest rate – The Company uses the market yield on U.S. Treasury securities at five years with constant maturity, representing the current expected life of stock options in years.

Expected life – The Company uses historical data to estimate the expected life of a stock option.

Historical volatility – The Company uses a trailing five year from grant date to determine volatility.

Stock Option Plans

During 1998, the Company established the Stock Option and Restricted Stock Purchase Plan (the “1998 Plan”). Under the 1998 Plan, the Board of Directors could issue incentive stock options or nonqualified stock options or other equity-based awards in respect of up to 5,850,000 shares of common stock. The 2000 Stock Incentive Plan (the “2000 Plan”) succeeded the 1998 Plan. Under the 2000 Plan, the options which had been outstanding under the 1998 Plan were incorporated in the 2000 Plan increasing the number of shares available for issuance under the plan by approximately 4,150,000, thereby reserving for issuance 10,000,000 shares of common stock in the aggregate.

The Company established the 2009 Stock Incentive Plan (as amended and restated, the “2009 Plan”) as a successor to the 2000 Plan. Under the 2009 Plan, the options which had been outstanding under the 2000 Plan were incorporated into the 2009 Plan and the Company increased the number of shares available for issuance under the plan by 6,000,000. The Company amended the 2009 Plan (the “Amended 2009 Plan”) effective June 7, 2012. The Amended 2009 Plan increased the number of shares authorized for issuance under the plan by an additional 4,250,000.

On June 2, 2017, the Company's Board of Directors amended and restated the Amended 2009 Plan effective April 30, 2017. The amended and restated plan increased the number of shares authorized for issuance under the plan by an additional 4,000,000, thereby reserving for issuance 27,817,744 shares of common stock in the aggregate. Options to acquire common stock granted thereunder have 10-year terms. As of June 30, 2018, approximately 2.2 million shares of common stock were reserved for issuance under the Amended 2009 Plan (taking into account all option exercises and other equity award settlements through June 30, 2018).

Employee Stock Purchase Plan

In June 2010, the Company's stockholders approved the 2010 Employee Stock Purchase Plan with 1,000,000 shares of common stock initially reserved for issuance. Subject to stockholder approval, which was obtained on June 2, 2017, the Company's Board of Directors amended and restated the 2010 Employee Stock Purchase Plan effective April 30, 2017. The amended and restated plan increased the number of shares authorized for issuance under the plan by an additional 1,000,000, thereby reserving for issuance 2,000,000 shares of common stock in the aggregate. As of June 30, 2018, approximately 0.9 million shares of common stock were reserved for issuance under the Employee Stock Purchase Plan (taking into account all share purchases through June 30, 2018).

Inducement Plan

During January 2018, the Company established the Inducement Plan (the “2018 Plan”). Under the 2018 Plan, the Board of Directors can issue incentive stock options or nonqualified stock options or other equity-based awards in respect of up to 1,500,000 shares of common stock. On April 25, 2018, the Company's Board of Directors amended and restated

the 2018 Plan (the "Amended 2018 Plan"). The Amended 2018 Plan increased the number of shares authorized for issuance under the plan by

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an additional 500,000 shares, thereby reserving for issuance 2,000,000 shares of common stock in the aggregate. As of June 30, 2018, approximately 0.6 million shares of common stock were reserved for issuance under the Amended 2018 Plan (taking into account all option exercises and other equity award settlements through June 30, 2018).

Stock Option Activity

A summary of the Company's stock option activity and weighted average exercise prices follows:

	Stock Option Activity			Aggregate Intrinsic Value (in thousands)
	Options (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	
Balance outstanding at December 31, 2017	7,959	\$ 10.71		
Granted	1,765	14.10		
Exercised	(2,273)	10.73		
Cancelled or expired	(274)	9.49		
Balance outstanding at June 30, 2018	7,177	\$ 11.58	7.03	\$ 68,433
Options vested and expected to vest	6,189	\$ 11.46	6.66	\$ 59,773
Options exercisable at June 30, 2018	3,658	\$ 11.04	4.99	\$ 36,802

The total fair value of stock options exercised during the six months ended June 30, 2018 was approximately \$12.1 million. As of June 30, 2018, there was approximately \$17.2 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements. That cost is expected to be recognized over a weighted average period of approximately 3.0 years.

The following table summarizes information about outstanding and vested stock options as of June 30, 2018:

Range of Exercise Prices	Options Outstanding		Weighted-Average Exercise Price	Options Exercisable	
	Number of Shares Outstanding (in thousands)	Weighted-Average Remaining Contractual Life (in years)		Number of Shares (in thousands)	Weighted-Average Exercise Price
\$1.79 - \$7.45	708	5.26	\$ 6.33	485	\$ 6.01
\$7.60 - \$7.60	748	8.39	7.60	214	7.60
\$7.95 - \$9.55	830	6.59	9.20	583	9.21
\$9.90 - \$10.13	727	6.03	10.09	650	10.09
\$10.31 - \$11.95	726	7.50	11.23	377	10.84
\$11.96 - \$12.32	87	3.04	12.12	88	12.12
\$12.45 - \$12.45	930	9.63	12.45	—	—
\$12.46 - \$13.59	810	4.07	13.28	747	13.26
\$14.30 - \$15.85	726	9.33	14.60	16	15.77
\$15.96 - \$21.75	885	6.60	17.87	498	17.27
	7,177	7.03	\$ 11.58	3,658	\$ 11.04

Restricted Stock Unit Activity

A summary of the Company's restricted stock units ("RSUs") activity and weighted average exercise prices follows:

	Restricted Stock Unit Activity		
	Weighted		Aggregate
	Number	Average	Fair Value
	of	Grant	(in
	Shares	Date Fair	thousands)
	(in	Value	(in
	thousands)	Per	thousands)
		Share)	
Balance outstanding at December 31, 2017	1,123	\$ 9.03	\$ —
Awarded	1,843	15.13	—
Released	(251)	9.05	—
Forfeited	(107)	8.02	—
Non-vested and outstanding at June 30, 2018	2,608	\$ 13.38	\$ 55,026
Expected to vest	1,798	\$ 12.80	\$ 37,936

RSUs granted to employees generally vest over a four-year period or upon achievement of certain performance conditions. In accordance with ASU 2017-09, as of June 30, 2018, total unrecognized compensation cost, adjusted for estimated forfeitures, related to nonvested RSUs was approximately \$33.4 million and the weighted-average remaining vesting period was 3 years.

11. Restructuring

The Company's restructuring costs related to wind-down and severance costs associated with re-prioritizing and reallocating resources to focus on areas showing high growth potential. The expense associated with this restructuring was approximately \$1.9 million and \$2.1 million during the three months ended June 30, 2018 and 2017, respectively and approximately \$2.1 million and \$2.3 million during the six months ended June 30, 2018 and 2017, respectively. The restructuring liability was approximately \$2.6 million as of June 30, 2018 and \$2.3 million as of December 31, 2017. It is classified as accrued expenses and other current liabilities on the condensed consolidated balance sheets. The following table presents the detail of the liability for the Company's restructuring charges for the periods presented (amounts in thousands):

	June 30, December	
	2018	31, 2017
Balance, Beginning of the year	\$2,338	\$ 2,551
Severance and other associated costs	2,084	648
Cash payments	(1,845)	(2,807)
Wind down cost legacy platform	—	1,946
Balance, End of period	\$2,577	\$ 2,338

The following table presents the detail of expenses for the Company's restructuring charges for the three months ended June 30, 2018 (amounts in thousands):

	June	June
	30,	30,
	2018	2017
Severance and other associated costs	\$1,906	\$289
Wind down cost legacy platform	—	1,787
Total restructuring costs	\$1,906	\$2,076

The following table presents the detail of expenses for the Company's restructuring charges for the six months ended June 30, 2018 (amounts in thousands):

	June 30, 2018	June 30, 2017
Severance and other associated costs	\$2,084	\$399
Wind down cost legacy platform	—	1,916
Total restructuring costs	\$2,084	\$2,315

12. Legal Matters

The Company previously filed an intellectual property suit against [24]7 Customer, Inc. in the Southern District of New York on March 6, 2014 seeking damages on the grounds that [24]7 reverse engineered and misappropriated the Company's technology to develop competing products and misused the Company's business information. On June 22, 2015, [24]7 Customer, Inc. filed suit against the Company in the Northern District of California alleging patent infringement. On December 7, 2015, [24]7 Customer Inc. filed a second patent infringement suit against the Company, also in the Northern District of California. On March 16, 2017, the New York case was voluntarily transferred and consolidated with the two California cases in the Northern District of California for all pre-trial purposes. Recent rulings by both the Court and the United States Patent Office in the Company's favor have invalidated the majority of [24]7 patents that were asserted in the patent cases. Trial for the Company's intellectual property and other claims asserted against [24]7 in the original litigation is currently set for April 2019. The Company believes the claims filed by [24]7 are without merit and intends to defend them vigorously.

The Company routinely assesses all of its litigation and threatened litigation as to the probability of ultimately incurring a liability, and records its best estimate of the ultimate loss in situations where the Company assesses the likelihood of loss as probable.

From time to time, the Company is involved in or subject to legal, administrative and regulatory proceedings, claims, demands and investigations arising in the ordinary course of business, including direct claims brought by or against the Company with respect to intellectual property, contracts, employment and other matters, as well as claims brought against the Company's customers for whom the Company has a contractual indemnification obligation. The Company accrues for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Significant judgment is required in both the determination of probability and the determination as to whether a loss is reasonably estimable. In addition, in the event the Company determines that a loss is not probable, but is reasonably possible, and it becomes possible to develop what the Company believes to be a reasonable range of possible loss, then the Company will include disclosure related to such matter as appropriate and in compliance with ASC 450. The accruals or estimates, if any, resulting from the foregoing analysis, are reviewed at least quarterly and adjusted to reflect the impact of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular matter. To the extent there is a reasonable possibility that the losses could exceed the amounts already accrued, the Company will, as applicable, adjust the accrual in the period the determination is made, disclose an estimate of the additional loss or range of loss, indicate that the estimate is immaterial with respect to its financial statements as a whole or, if the amount of such adjustment cannot be reasonably estimated, disclose that an estimate cannot be made.

From time to time, third parties assert claims against the Company regarding intellectual property rights, privacy issues and other matters arising in the ordinary course of business. Although the Company cannot be certain of the outcome of any litigation or the disposition of any claims, nor the amount of damages and exposure, if any, that the Company could incur, the Company currently believes that the final disposition of all existing matters will not have a material adverse effect on our business, results of operations, financial condition or cash flows. In addition, in the ordinary course of business, the Company is also subject to periodic threats of lawsuits, investigations and claims. Regardless of the outcome, litigation can have an adverse impact on the Company because of defense and settlement costs, diversion of management resources and other factors.

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

General

Our discussion and analysis of our financial condition and results of operations is based upon our condensed consolidated financial statements, which are prepared in conformity with accounting principles generally accepted in the United States of America. As such, we are required to make certain estimates, judgments and assumptions that management believes are reasonable based upon the information available. We base these estimates on our historical experience, future expectations and various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for our judgments that may not be readily apparent from other sources. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the condensed consolidated financial statements and the reported amounts of revenue and expenses during the reporting periods. These estimates and assumptions relate to estimates of the carrying amount of goodwill, intangibles, depreciation, stock based-compensation, valuation allowances for deferred income taxes, accounts receivable, the expected term of a customer relationship, accruals and other factors. We evaluate these estimates on an ongoing basis. Actual results could differ from those estimates under different assumptions or conditions, and any differences could be material.

Overview

LivePerson was incorporated in the State of Delaware in November 1995 and the LivePerson service was introduced in November 1998. LivePerson makes life easier by transforming how people communicate with brands. LiveEngage, the Company's enterprise-class, cloud-based platform, enables businesses and consumers to connect through conversational interfaces, such as in-app and mobile messaging, while leveraging bots and Artificial Intelligence (AI) to increase efficiency. As consumers have reoriented their digital lives around the smartphone, messaging apps have become their preferred communication channel to connect with each other. LivePerson allows brands to align with this new consumer preference, and deploy messaging at scale for customer care, marketing and sales, instead of requiring that consumers use email or call a 1-800 number. More than 18,000 businesses, including Adobe, Citibank, EE, HSBC, IBM, L'Oreal, Orange, PNC, and The Home Depot employ our technology to keep pace with rising customer service expectations and to align with preferences for digital communication channels.

We are organized into two operating segments: Business and Consumer. The Business segment enables brands to leverage LiveEngage's sophisticated intelligence engine to connect with consumers through an integrated suite of mobile and online business messaging technologies. The Consumer segment facilitates online transactions between independent service providers ("Experts") and individual consumers ("Users") seeking information and knowledge for a fee via mobile and online messaging.

In order to sustain growth in these segments, our strategy is to expand our position as the leading provider of online and mobile messaging solutions that transform how people communicate with brands. To accomplish this, we are focused on the following current initiatives:

Strengthening Our Position in both Existing and New Markets and Growing Our Recurring Revenue Base.

LivePerson plans to continue to develop its market position by increasing its customer base, and expanding within its installed base. We will continue to focus primarily on key target markets: automotive, financial services, retail, technology, telecommunications, and travel/hospitality within both our enterprise and mid-market sectors, as well as the small business (SMB) sector. Healthcare, insurance, real estate and energy utilities are new target industries and natural extensions of our primary target markets. We plan to leverage our LiveEngage platform to replace a portion of calls traditionally made to 1-800 numbers with text and mobile messaging, and to increase adoption of real-time, campaign-based messaging across our customer's online properties. We intend to collaborate with our large installed customer base to optimize the value and effectiveness that brands derive from our services. We are also focused on strengthening our recurring revenue stream by signing larger, long-term, and more strategic deals.

One of the key ways we are developing our market position is by hosting customer summits for executive level attendees from our targeted enterprise customer base and prospects. These customer summits feature existing customers that have demonstrated strong success with messaging and bots on LiveEngage. We believe that scaled reference customers advocating the adoption of messaging on LiveEngage to targeted peer groups will be a key driver of our growth. In 2017, we increased the pacing and scale of these summits, a pattern that we have continued in 2018.

Fuel Increased Usage by Expanding Messaging Channels, Use Cases and Interaction Types. LiveEngage currently supports numerous messaging endpoints including branded mobile apps, mobile and desktop web browsers, IVRs, SMS, Facebook Messenger and LINE. We intend to increase the number of endpoints supported by the LiveEngage platform to include additional third-party social apps and device-based systems. We also intend to broaden the use cases of LiveEngage across our customer base, to support care, sales, marketing and retail footprints. In addition, LivePerson continues to expand the breadth of interaction types available to customers on the platform. For example, in addition to our broad suite of messaging and real-time chat

technologies, customers have access to content delivery, analytics, cobrowse, and PCI compliance, as well as proprietary and third-party bot offerings. LivePerson offers a platform pricing model, which provides businesses access to our entire suite of messaging technologies across their entire agent pool for a pre-negotiated cost per interaction. We believe this model will lead to growth opportunities for LivePerson as customers adopt new messaging channels, use cases and interaction types.

Leverage Partners to Enhance our Offering. In addition to developing our own applications, we continue to cultivate a partner ecosystem capable of offering additional applications and services to our customers. The pace of our ecosystem expansion has accelerated in 2018, as we built on our existing integrations with Facebook Messenger and LINE, by adding integrations to Apple Business Chat, Google Rich Business Messenger, WhatsApp, Alexa and Google Home. These popular conversational interfaces enable brands the opportunity to connect to millions of consumers, which in turn can increase traffic on our platform.

Our offering is vendor agnostic, empowering our customers to manage a mix of different bots, human agents and technologies from one control panel, thereby optimizing contact center efficiency. In 2017, LivePerson launched the LiveEngage for Bots program and we have subsequently integrated LiveEngage with multiple artificial intelligence/bots vendors, including IBM Watson. LivePerson's proprietary and third-party AI/bots enable brands to partially or fully automate communications with their customers. In addition, we have opened up access to our platform and our products with application programming interfaces (APIs) that allow third parties to develop on top of our platform. Customers and partners can utilize these APIs to build our capabilities into their own applications and to enhance our applications with their services. In 2017, we allocated additional resources to supporting partners and we expect this investment to increase as our partner network expands.

Maintaining Market Leadership in Technology and Security Expertise. As described above, we are devoting significant resources to creating new products and enabling technologies designed to accelerate innovation. In order to better support our customers and to attract the best talent, LivePerson is globalizing research and development. We now have tech centers in Israel; Mannheim, Germany; New York; Atlanta; Mountain View, California; and Seattle. We evaluate emerging technologies and industry standards and continually update our technology in order to retain our leadership position in each market we serve. We monitor legal and technological developments in the area of information security and confidentiality to ensure our policies and procedures meet or exceed the demands of the world's largest and most demanding corporations. We believe that these efforts will allow us to effectively anticipate changing customer and consumer requirements in our rapidly evolving industry.

International Presence. LivePerson is focused on expanding its international revenue contribution, which increased to 37% of total revenue in 2017, from 34% in 2016 and 33% in 2015. LivePerson generated positive results from previous investments in direct sales and services personnel in the United Kingdom and Western Europe. We also continued to focus on expanding our presence in the Asia Pacific region, leveraging our relationships with partners.

Continuing to Build Brand Recognition. As a pioneer of brand-to-consumer digital messaging, LivePerson enjoys strong brand recognition and credibility. We continue to develop relationships with the media, industry analysts and relevant business associations to enhance awareness of our leadership within the care, sales, tech and marketing industries. With a vision of becoming the leader in messaging, we've hosted several private executive events for our customers and prospects, highlighting our expertise and the breadth of our services. These private executive events have led us to close several high-profile deals and we are continuing them throughout 2018. Our focus on connecting large enterprise businesses and their millions of consumers securely and at scale is a primary differentiator for LivePerson and a key component of our marketing strategy. We strategically target decision makers and influencers within several key vertical markets, leveraging customer successes to generate increased awareness and demand for brand-to-consumer messaging. In addition, our brand name may also be visible to both business users and consumers on a brand's website, within the dialog messaging window. We also engage in digital marketing campaigns that promote our brand on web searches and third-party sites.

Increasing the Value of Our Service to Our Customers. Leveraging LiveEngage to shift communication between consumers and brands from 1-800 number calls to AI and human-powered messaging is the most important initiative in LivePerson's history. We believe that adoption of LiveEngage will align brands with consumer communication preferences, improve the customer experience and reduce contact center costs. Our platform strategy makes available

the full suite of LivePerson's capabilities through a single solution. In addition, the open architecture of LiveEngage will enable LivePerson to rapidly add new capabilities either directly or through partners. For example, we see opportunities for additional efficiencies in the contact center through the integration of artificial intelligence and bots. Because we directly manage the server infrastructure, we can make new features available to our customers immediately upon release, without customer or end-user installation of software or hardware. Our strategy is to continue to enhance the LiveEngage messaging platform and to leverage the substantial amount of mobile and online consumer data we collect, with the aim of increasing agent efficiency, decreasing customer care costs, improving the customer experience and increasing customer lifetime value.

Evaluating Strategic Alliances and Acquisitions When Appropriate. We have successfully integrated several acquisitions over the past decade. While we have in the past, and may from time to time in the future, engage in discussions regarding acquisitions or strategic transactions or to acquire other companies that can accelerate our growth or broaden our product offerings, we currently have no binding commitments with respect to any future acquisitions or strategic transactions.

Key Metrics

Financial overview of the three months ended June 30, 2018 compared to the three months ended June 30, 2017:

Total revenue increased 14% to \$61.7 million from \$54.1 million

Revenue from our Business segment increased 14% to \$56.7 million from \$49.6 million.

Gross profit margin increased to 74% from 72%.

Cost and expenses increased 14% to \$69.5 million from \$60.8 million.

Net loss increased to \$8.3 million from net loss of \$7.5 million.

Average annual revenue per enterprise and mid-market customer was greater than \$255,000 over the trailing twelve months ended June 30, 2018, as compared to greater than \$205,000 for the trailing twelve months ended June 30, 2017.

The revenue retention rate for full service customers on LiveEngage was greater than 100% over the trailing twelve months ended June 30, 2018, continuing the trend of 100% plus revenue retention that we reported in 2017. Revenue retention rate measures the percentage of revenue retained at quarter end, from full service customers that were on LiveEngage at the same period a year ago.

Adjusted EBITDA and Adjusted Net Income

To provide investors with additional information regarding our financial results, we have disclosed adjusted EBITDA and adjusted net income, which are non-GAAP financial measures. The tables below present a reconciliation of adjusted EBITDA and adjusted net income to net loss, the most directly comparable GAAP financial measures. We have included adjusted EBITDA and adjusted net income in this Quarterly Report on Form 10-Q because these are key measures used by our management and board of directors to understand and evaluate our core operating performance and trends, to prepare and approve our annual budget and to develop short and long-term operational plans. In particular, the exclusion of certain expenses in calculating adjusted EBITDA and adjusted net income can provide a useful measure for period-to-period comparisons of our core business. Additionally, adjusted EBITDA is a key financial measure used by the compensation committee of our board of directors in connection with the payment of bonuses to our executive officers. Accordingly, we believe that adjusted EBITDA and adjusted net income provide useful information to investors and others in understanding and evaluating our operating results in the same manner as our management and board of directors.

Our use of adjusted EBITDA has limitations as an analytical tool, and you should not consider it in isolation or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are:

although depreciation and amortization are non-cash charges, the assets being depreciated and amortized may have to be replaced in the future, and adjusted EBITDA does not reflect cash capital expenditure requirements for such replacements or for new capital expenditure requirements;

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

adjusted EBITDA does not consider the potentially dilutive impact of equity-based compensation;

adjusted EBITDA does not consider the potentially dilutive impact of restructuring cost;

adjusted EBITDA does not consider the potentially dilutive impact of other non-recurring costs;

adjusted EBITDA does not reflect tax payments that may represent a reduction in cash available to us; and

other companies, including companies in our industry, may calculate adjusted EBITDA differently, which reduces its usefulness as a comparative measure.

Because of these limitations, you should consider adjusted EBITDA alongside other financial performance measures, including various cash flow metrics, net income (loss) and our other GAAP results. The following table presents a reconciliation of adjusted EBITDA for each of the periods indicated (amounts in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,		
	2018	2017	2018	2017	
Reconciliation of Adjusted EBITDA					
GAAP net loss	\$(8,321)	\$(7,533)	\$(11,524)	\$(13,209)	
Amortization of purchased intangibles	711	1,429	1,422	2,860	
Stock-based compensation	3,826	2,347	6,264	4,260	
Depreciation	3,428	3,045	6,786	5,838	
Other non-recurring costs	1,768	(1) 1,534	(2) 3,038	(3) 3,358	(2)
Restructuring costs	1,906	(4) 2,075	(5) 2,084	(4) 2,315	(6)
Provision for income taxes	536	673	47	1,744	
Other income, net	(31)	99	(160)	(221)	
Adjusted EBITDA	\$3,823	\$3,669	\$7,957	\$6,945	

(1) Includes litigation costs of \$1.2 million, consulting costs of \$0.4 million, and executive relocation costs of \$0.2 million for the three months ended June 30, 2018.

(2) Includes litigation costs of \$1.5 million and \$3.4 million for the three and six months ended June 30, 2017.

(3) Includes litigation costs of \$2.1 million, consulting costs of \$0.4 million, executive recruitment costs of \$0.3 million, and executive relocation costs of \$0.2 million for the six months ended June 30, 2018.

(4) Includes severance costs of \$1.9 million and \$2.1 million for the three and six months ended June 30, 2018.

(5) Includes wind down costs of legacy platform of \$1.8 million and severance costs of \$0.3 million for the three months ended June 30, 2017.

(6) Includes wind down costs of legacy platform of \$1.9 million and severance costs of \$0.4 million for the six months ended June 30, 2017.

Our use of adjusted net income has limitations as an analytical tool, and you should not consider it in isolation or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are:

although amortization is a non-cash charge, the assets being amortized may have to be replaced in the future, and adjusted net income does not reflect cash capital expenditure requirements for such replacements or for new capital expenditure requirements;

adjusted net income does not consider the potentially dilutive impact of equity-based compensation;

adjusted net income does not consider the potentially dilutive impact of restructuring cost;

adjusted net income does not consider the potentially dilutive impact of other non-recurring costs;

adjusted net income does not consider the potentially dilutive impact of deferred tax asset valuation allowance; and other companies, including companies in our industry, may calculate adjusted net income differently, which reduces its usefulness as a comparative measure.

Because of these limitations, you should consider adjusted net income alongside other financial performance measures, including various cash flow metrics, net loss and our other GAAP results. The following table presents a reconciliation of adjusted net (loss) income for each of the periods indicated (amounts in thousands):

	Three Months Ended		Six Months Ended June		
	June 30, 2018	2017	30, 2018	2017	
Reconciliation of Adjusted Net Income					
Pre-tax GAAP loss	\$(7,785)	\$(6,860)	\$(11,477)	\$(11,465)	
Amortization of purchased intangibles	711	1,429	1,422	2,860	
Stock-based compensation	3,826	2,347	6,264	4,260	
Other non-recurring costs	1,768	(1) 1,534	(2) 3,038	(3) 3,358	(2)
Restructuring costs	1,906	(4) 2,075	(5) 2,084	(4) 2,315	(6)
Pre-tax adjusted net income	426	525	1,331	1,328	
Income tax effect of non-GAAP items ⁽⁷⁾	(107)	(184)	(333)	(465)	
Adjusted net income	\$319	\$341	\$998	\$863	

(1) Includes litigation costs of \$1.2 million, consulting costs of \$0.4 million, and executive relocation costs of \$0.2 million for the three months ended June 30, 2018.

(2) Includes litigation costs of \$1.5 million and \$3.4 million for the three and six months ended June 30, 2017.

(3) Includes litigation costs of \$2.1 million, consulting costs of \$0.4 million, executive recruitment costs of \$0.3 million, and executive relocation costs of \$0.2 million for the six months ended June 30, 2018.

(4) Includes severance costs of \$1.9 million and \$2.1 million for the three and six months ended June 30, 2018.

(5) Includes wind down costs of legacy platform of \$1.8 million and severance costs of \$0.3 million for the three months ended June 30, 2017.

(6) Includes wind down costs of legacy platform of \$1.9 million and severance costs of \$0.4 million for the six months ended June 30, 2017.

(7) The Company applies a standardized tax rate of 25% for the three and six months ended June 30, 2018. The Company applied a standardized tax rate of 35% for the three and six months ended June 30, 2017.

Critical Accounting Policies and Estimates

Our condensed consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. As such, we are required to make certain estimates, judgments and assumptions that management believes are reasonable based upon the information available. We base these estimates on our historical experience, future expectations and various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for our judgments that may not be readily apparent from other sources. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting periods.

We believe that the assumptions and estimates associated with revenue recognition, depreciation, stock-based compensation, accounts receivable, the valuation of goodwill and intangible assets, income taxes and legal contingencies have the greatest potential impact on our consolidated financial statements. We evaluate these estimates on an ongoing basis. Actual results could differ from those estimates under different assumptions or conditions, and any differences could be material. The significant accounting policies which we believe are the most critical to aid in fully understanding and evaluating the reported consolidated financial results include the following:

Revenue Recognition

The majority of the Company's revenue is generated from monthly service revenues and related professional services from the sale of the LivePerson services. Revenues are recognized when control of these services is transferred to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for those services.

The Company determines revenue recognition through the following steps:

- identification of the contract, or contracts, with a customer;
- identification of the performance obligations in the contract;
- determination of the transaction price;
- allocation of the transaction price to the performance obligations in the contract; and
- recognition of revenue when, or as, the Company satisfies a performance obligation.

Total revenue of \$61.7 million and \$119.9 million recognized during the three months and six months ended June 30, 2018, respectively, under Topic 606, was not materially different from what would have been recognized under Topic 605.

Hosted Services- Business Revenue

Hosted Services Business revenue is reported at the amount that reflects the ultimate consideration expected to be received and primarily consist of fees that provide customers access to LiveEngage, our enterprise-class, cloud-based platform. We have determined such access represents a stand-ready service provided continually throughout the contract term. As such, control and satisfaction of this stand-ready performance obligation is deemed to occur over time. We recognize this revenue over time on a ratable basis over the contract term, beginning on the date that access to the LiveEngage platform is made available to the customer. The passage of time is deemed to be the most faithful depiction of the transfer of control of the services as the customer simultaneously receives and consumes the benefit provided by the our performance. Subscription contracts are generally one year or longer in length, billed, monthly, quarterly or annually in advance. There is no significant variable consideration related to these arrangements. Additionally, for certain of the our larger customers, we may provide call center labor through an arrangement with one or more of several qualified vendors. For most of these customers, we pass the fee we incur with the labor provider and the fee for the hosted services through to our customers in the form of a fixed fee for each order placed via our online engagement solutions. For these Pay for Performance ("PFP") arrangements in accordance with ASC-606, "Principal Agent Considerations", we act as a principal in a transaction if it controls the specified goods or services before they are transferred to the customer.

Professional Services Revenues

Professional services revenue primarily consists of fees for deployment and optimization services, as well as training delivered on an on-demand basis which is deemed to represent a distinct stand-ready performance obligation. Professional Services Revenues are reported at the amount that reflects the ultimate consideration we expect to receive in exchange for such services. Control for the majority of our Professional Services contracts passes over time to the customer and is recognized ratably over the contracted period, as the passage of time is deemed to be the most faithful depiction of the transfer of control. For certain deployment services, which are not deemed to represent a distinct performance obligation, revenue will be recognized in the same manner as the fee for access to the LiveEngage platform and as such will be recognized on a straight-line basis over the contract term. For services billed on a fixed price basis, revenue is recognized over time based on the proportion performed using inputs as the measure of progress toward complete satisfaction of the performance obligation. Professional service contracts are generally one year or longer in length, billed, monthly, quarterly or annually in advance. There is no significant variable consideration related to these arrangements.

Contracts with Multiple Performance Obligations

Some of our contracts with customers contain multiple performance obligations. For these contracts, we account for individual performance obligations separately if they are distinct. The transaction price is allocated to the separate performance obligations on a relative standalone selling price basis. We determine the standalone selling prices based on our overall pricing objectives, taking into consideration market conditions and other factors, including the value of our contracts, the cloud applications sold, and the number and types of users within our contracts.

Hosted Services- Consumer Revenue

For revenue from our Consumer segment generated from online transactions between Experts and Users, revenue is recognized at an amount net of Expert fees in accordance with ASC 606, "Principal Agent Considerations," due primarily to the fact that the Expert is the primary obligor. Additionally, we perform as an agent without any risk of

loss for collection, and are not involved in selecting the Expert or establishing the Expert's fee. We collect a fee from the consumer and retains a portion of the fee, and then remit the balance to the Expert. Revenue from these transactions is recognized at the point in time when the transaction is complete and no significant performance obligations remain.

Deferred Revenues

We record deferred revenues when cash payments are received or due in advance of our performance. The increase in the deferred revenue balance for the six months ended June 30, 2018 is primarily driven by cash payments received or due in advance of satisfying our performance obligations, partially offset by \$26.2 million of revenues recognized that were included in the deferred revenue balance as of December 31, 2017.

Stock-Based Compensation

We follow ASC 718-10, “Stock Compensation,” which addresses the accounting for transactions in which an entity exchanges its equity instruments for goods or services, with a primary focus on transactions in which an entity obtains employee services in share-based payment transactions. ASC 718-10 requires measurement of the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award (with limited exceptions). Incremental compensation costs arising from subsequent modifications of awards after the grant date must be recognized.

As of June 30, 2018, there was approximately \$17.2 million of total unrecognized compensation cost related to nonvested stock options. That cost is expected to be recognized over a weighted average period of approximately 3.0 years. As of June 30, 2018, there was approximately \$33.4 million of total unrecognized compensation cost related to nonvested restricted stock units. That cost is expected to be recognized over a weighted average period of approximately 3.0 years.

Accounts Receivable

Our customers are located primarily in the United States. We perform ongoing credit evaluations of our customers’ financial condition (except for customers who purchase the LivePerson services by credit card via Internet download) and have established an allowance for doubtful accounts based upon factors surrounding the credit risk of customers, historical trends and other information that we believe to be reasonable, although they may change in the future. If there is a deterioration of a customer’s credit worthiness or actual write-offs are higher than our historical experience, our estimates of recoverability for these receivables could be adversely affected. Although our large number of customers limits our concentration of credit risk we do have several large customers. If we experience a significant write-off from one of these large customers, it could have a material adverse impact on our condensed consolidated financial statements. No single customer accounted for or exceeded 10% of our total revenue in the three and six months ended June 30, 2018 and 2017. No customer accounted for approximately 10% of accounts receivable as of June 30, 2018 and December 31, 2017.

A large proportion of our receivables are due from larger corporate customers that typically have longer payment cycles. We base our allowance for doubtful accounts on specifically identified credit risks of customers, historical trends and other information that we believe to be reasonable. Receivables are written-off and charged against its recorded allowance when we have exhausted collection efforts without success. We adjust our allowance for doubtful accounts when accounts previously reserved have been collected. During the six months ended June 30, 2018, our allowance for doubtful accounts increased by \$0.4 million to approximately \$1.6 million. During 2017, we decreased our allowance for doubtful accounts by \$0.4 million to approximately \$1.3 million.

Goodwill

In accordance with ASC 350, “Goodwill and Other Intangible Assets,” goodwill and indefinite-lived intangible assets are not amortized, but reviewed for impairment upon the occurrence of events or changes in circumstances that would reduce the fair value below its carrying amount. Goodwill is required to be tested for impairment at least annually. In September 2011, FASB issued ASU No. 2011-08, Intangibles — Goodwill and Other (Topic 350). ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is “more likely than not” that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. If it is determined that the fair value of a reporting unit is more likely than not to be less than its carrying value (including unrecognized intangible assets) then it is necessary to perform the second step of the goodwill impairment test. The second step of the goodwill impairment test is judgmental in nature and often involves the use of significant estimates and assumptions. Similarly, estimates and assumptions are used in determining the fair value of other intangible assets. These estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of any such charge. We perform internal valuation analysis and consider other market information that is publicly available. Estimates of fair value are primarily determined using discounted cash flows and market comparisons. These approaches use significant estimates and assumptions including projected future cash flows (including timing), discount rates reflecting the risk inherent in future cash flows, perpetual growth rates, determination of appropriate market comparables and the determination of whether a

premium or discount should be applied to such comparables.

We evaluate for goodwill impairment annually at September 30th. At the end of the third quarter of 2017, we determined that it was not more-likely that the fair value of the reporting units are less than their carrying amount.

Accordingly, we did not perform the two-step goodwill impairment test.

Impairment of Long-Lived Assets

In accordance with ASC 360-10, "Accounting for the Impairment or Disposal of Long-lived Assets," long-lived assets, such as property, plant and equipment and purchased intangibles subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. The amount of any impairment

is measured as the difference between the carrying value and the fair value of the impaired asset. We do not have any long-lived assets, including intangible assets, which we consider to be impaired.

Legal Contingencies

We are subject to legal proceedings and litigation arising in the ordinary course of business. Periodically, we evaluate the status of each legal matter and assess our potential financial exposure. If the potential loss from any legal proceeding or litigation is considered probable and the amount can be reasonably estimated, we accrue a liability for the estimated loss. Significant judgment is required to determine the probability of a loss and whether the amount of the loss is reasonably estimable. The outcome of any proceeding is not determinable in advance. As a result, the assessment of a potential liability and the amount of accruals recorded are based only on the information available at the time. As additional information becomes available, we reassess the potential liability related to the legal proceeding or litigation, and may revise our estimates. Any revisions could have a material effect on our results of operations. See Note 12, Legal Matters, of the Notes to the Condensed Consolidated Financial Statements for additional information on our legal proceedings and litigation.

Recently Issued Accounting Standards

See Note 1 of the Notes to Condensed Consolidated Financial Statements for a full description of recently issued accounting standards.

Recently Adopted Accounting Pronouncements

See Note 1 of the Notes to Condensed Consolidated Financial Statements for a full description of recently adopted accounting pronouncements.

Revenue

The majority of our revenue is generated from monthly service revenues and related professional services from the sale of the LivePerson services. We charge a monthly, quarterly or annual fee, which varies by service and customer usage. The majority of our larger customers also pay a professional services fee related to implementation and ongoing optimization services. A large proportion of our revenue from new customers comes from large corporations. These companies typically have more significant implementation requirements and more stringent data security standards. Such customers also have more sophisticated data analysis and performance reporting requirements, and are likely to engage our professional services organization to provide such analysis and reporting on a recurring basis. Revenues are recognized when control of the promised goods or services is transferred to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for those goods or services.

Revenue from our Business segment accounted for 92% of total revenue for the three and six months ended June 30, 2018 and 2017. Revenue attributable to our monthly hosted Business services accounted for 85% and 87% of total Business revenue for the three and six months ended June 30, 2018, respectively. Revenue attributable to our monthly hosted Business services accounted for 89% of total Business revenue for the three and six months ended June 30, 2017. Our service agreements typically have twelve month terms and, in some cases, are terminable or may terminate upon 30 to 90 days' notice without penalty. Given the time required to schedule training for our customers' operators and our customers' resource constraints, we have historically experienced a lag between signing a customer contract and recognizing revenue from that customer. Although this lag typically ranges from 30 to 90 days, it may take more or less time between contract signing and recognizing revenue in certain situations.

Revenue from our Consumer segment is generated from online transactions between Experts and Users and is recognized net of Expert fees and accounted for approximately 8% of total revenue for the three and six months ended June 30, 2018 and 2017.

We also have entered into contractual arrangements that complement our direct sales force and online sales efforts. These are primarily with call center service companies, pursuant to which LivePerson is paid a commission based on revenue generated by these service companies from our referrals. To date, revenue from such commissions has not been material.

Costs and Expenses

Our cost of revenue consists of:

- compensation costs relating to employees who provide customer support and implementation services to our customers;

- outside labor provider costs;
- compensation costs relating to our network support staff;
- depreciation of certain hardware and software;

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allocated occupancy costs and related overhead;
the cost of supporting our infrastructure, including expenses related to server leases, infrastructure support costs and Internet connectivity;
the credit card fees and related payment processing costs associated with consumer and self-service customers; and
amortization of certain intangibles.

Our sales and marketing expenses consist of compensation and related expenses for sales personnel and marketing personnel, online marketing, allocated occupancy costs and related overhead, advertising, marketing events, sales commissions, public relations, promotional materials, travel expenses and trade show exhibit expenses.

Our general and administrative expenses consist primarily of compensation and related expenses for executive, accounting, legal, information technology and human resources personnel, allocated occupancy costs and related overhead, professional fees, provision for doubtful accounts and other general corporate expenses.

Our product development expenses consist primarily of compensation and related expenses for product development personnel, allocated occupancy costs and related overhead, outsourced labor and expenses for testing new versions of our software. Product development expenses are charged to operations as incurred.

Non-Cash Compensation Expense

The net non-cash compensation amounts are as follows:

	Three Months Ended June 30, 2018		Six Months Ended June 30, 2018	
	2018	2017	2018	2017
	(in thousands)		(in thousands)	
Stock-based compensation expense	\$3,826	\$2,347	\$6,264	\$4,260

Results of Operations

We are organized into two operating segments for purposes of making operating decisions and assessing performance. The Business segment enables brands to leverage LiveEngage's sophisticated intelligence engine to connect with consumers through an integrated suite of mobile and online business messaging technologies. The Consumer segment facilitates online transactions between independent service providers ("Experts") and individual consumers ("Users") seeking information and knowledge for a fee via mobile and online messaging.

Comparison of the Three and Six Months Ended June 30, 2018 and 2017

Revenue

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(in thousands)			(in thousands)		
Revenue by Segment:						
Business	\$56,708	\$49,614	14 %	\$110,269	\$96,363	14 %
Consumer	4,952	4,460	11 %	9,632	8,630	12 %
Total	\$61,660	\$54,074	14 %	\$119,901	\$104,993	14 %

Business revenue increased by 14% to \$56.7 million and \$110.3 million in the three and six months ended June 30, 2018, respectively, from \$49.6 million and \$96.4 million in the comparable periods in 2017. This variance was primarily attributable to the increase in revenue from professional services of approximately \$3.0 million and \$3.7 million, in revenue from existing customers of approximately \$2.2 million and \$4.9 million, in revenue from new customers of approximately \$1.3 million and \$4.2 million, and in revenue that is variable principally based on pay for performance of approximately \$0.6 million and \$1.2 million, respectively.

In 2017, we had notified the majority of our customers about the end of life on the legacy offering, and not every legacy customer elected to move to LiveEngage. After we finished the migration of current customers from our old platform to our new LiveEngage platform, our focus shifted back to selling and expanding our base of messaging customers. We continued to see a decrease in existing customer cancellations quarter over quarter. During the fourth quarter 2017, we returned to year over year revenue growth. This trend continued into the first and second quarters of 2018.

Consumer revenue increased by 11% and 12% to \$5.0 million and \$9.6 million in the three and six months ended June 30, 2018, respectively, from \$4.5 million and \$8.6 million in the comparable periods in 2017. This variance is driven by an increase in price per minute and in volume of chat minutes.

Cost of Revenue - Business

Cost of revenue consists of compensation costs relating to employees who provide customer service to our customers, compensation costs relating to our network support staff, outside labor provider costs, the cost of supporting our server and network infrastructure, and allocated occupancy costs and related overhead.

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
Cost of revenue - business	\$15,086	\$14,206	6 %	\$28,004	\$27,112	3 %
Percentage of total revenue	24%	26 %		23 %	26 %	
Headcount (at period end):	234	229	2 %	234	229	2 %

Cost of revenue increased by 6% to \$15.1 million in the three months ended June 30, 2018, from \$14.2 million in the comparable period in 2017. This variance was primarily attributable to increases in outsourced labor and other business services of approximately \$1.0 million and in total compensation and related costs for customer service and network operations personnel of approximately \$0.7 million. This was partially offset by decreases in amortization expense of approximately \$0.7 million and in primary and backup server facilities and allocated overhead related to costs supporting our server and network infrastructure of approximately \$0.2 million.

Cost of revenue increased by 3% to \$28.0 million in the six months ended June 30, 2018, from \$27.1 million in the comparable period in 2017. This variance was primarily attributable to increases in outsourced labor and other business services of approximately \$1.4 million and in total compensation and related costs for customer service and network operations personnel of approximately \$1.0 million. This was partially offset by decreases in amortization expense of approximately \$1.3 million and in primary and backup server facilities and allocated overhead related to costs supporting our server and network infrastructure of approximately \$0.3 million.

Gross margin for our business segment increased to 73% and 75% in the three and six months ended June 30, 2018, respectively, from 71% and 72% in the comparable periods in 2017. The increase in gross margin was tied to our ability to operationalize cost savings by moving brands off of our legacy platform and realigning our go-to-market strategy around LiveEngage.

Cost of Revenue - Consumer

Cost of revenue consists of compensation costs relating to employees who provide customer service to Experts and Users, compensation costs relating to our network support staff, the cost of supporting our server and network infrastructure, credit card and transaction processing fees and related costs, and allocated occupancy costs and related overhead.

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
Cost of revenue - consumer	\$950	\$928	2 %	\$1,986	\$1,803	10 %
Percentage of total revenue	2 %	2 %		2 %	2 %	

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Headcount (at period end) 17 20 (15)% 17 20 (15)%

Cost of revenue remained relatively flat in the three months ended June 30, 2018, from the comparable period in 2017. This variance was primarily attributable to increases in depreciation expense and credit card processing fees offset by decreases in backup server facilities and allocated occupancy costs and overhead.

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Cost of revenue increased by 10% to \$2.0 million in the six months ended June 30, 2018, from \$1.8 million the comparable period in 2017. This variance was primarily attributable to increases in depreciation expense, salary and related employee expenses, and credit card processing fees partially offset by decreases in backup server facilities and allocated occupancy costs and overhead.

Sales and Marketing - Business

Our sales and marketing expenses consist of compensation and related expenses for sales and marketing personnel, as well as advertising, marketing events, public relations, trade show exhibit expenses and allocated occupancy costs and related overhead.

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
Sales and marketing - business	\$23,339	\$21,242	10 %	\$45,062	\$40,785	10 %
Percentage of total revenue	38 %	39 %		38 %	39 %	
Headcount (at period end):	315	287	10 %	315	287	10 %

Sales and marketing expenses increased by 10% to \$23.3 million in the three months ended June 30, 2018 from \$21.2 million in the comparable period in 2017. This variance was primarily attributable to increases in salaries and related costs for sales and marketing personnel of approximately \$1.2 million, outsourced labor and other business services of approximately \$0.8 million, and in recruiting expenses of approximately \$0.5 million. This was partially offset by decreases in marketing events, advertising, public relations, and tradeshow exhibit expenses of approximately \$0.4 million.

Sales and marketing expenses increased by 10% to \$45.1 million in the six months ended June 30, 2018 from \$40.8 million in the comparable period in 2017. This variance was primarily attributable to increases in outsourced labor and other business services of approximately \$1.8 million, in recruiting expenses of approximately \$1.2 million, in salaries and related costs for sales and marketing personnel of approximately \$0.7 million and in marketing events, advertising, public relations, and tradeshow exhibit expenses of approximately \$0.6 million.

We have realigned our go-to-market strategy around LiveEngage 2.0. Our outreach efforts are primarily focused on fostering a community of thought and industry leadership by targeting a few hundred of the world's largest brands through conference calls and events.

Sales and Marketing - Consumer

Our sales and marketing expenses consist of compensation and related expenses for marketing personnel, as well as online promotion, public relations and allocated occupancy costs and related overhead.

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
Sales and marketing - consumer	\$2,053	\$2,150	(5) %	\$4,461	\$4,307	4 %
Percentage of total revenue	3 %	4 %		4 %	4 %	
Headcount (at period end):	12	12	— %	12	12	— %

Sales and marketing expenses decreased by 5% to \$2.1 million in the three months ended June 30, 2018 from \$2.2 million in the comparable periods in 2017. This variance was primarily attributable to decreases in advertising and online expenses, partially offset by increases in salaries and related costs for sales and marketing personnel.

Sales and marketing expenses increased by 4% to \$4.5 million in the six months ended June 30, 2018 from \$4.3 million in the comparable periods in 2017. This variance was primarily attributable to increases in salaries and related costs for sales and marketing personnel partially offset by decreases in advertising and online expenses.

General and Administrative

Our general and administrative expenses consist of compensation and related expenses for executive, accounting, legal, human resources and administrative personnel, professional fees and other general corporate expenses.

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
General and administrative	\$11,499	\$10,437	10 %	\$21,622	\$20,130	7 %
Percentage of total revenue	19 %	19 %		18 %	19 %	
Headcount (at period end):	114	107	7 %	114	107	7 %

General and administrative expenses increased by 10% to \$11.5 million in the three months ended June 30, 2018 from \$10.4 million in the comparable period in 2017. This variance was primarily attributable to increases in total compensation and related employee expenses of approximately \$0.7 million, in business services and outsourced labor of approximately \$0.3 million, and a net increase in non-recurring costs of approximately \$0.3 million. This was partially offset by decreases in allocated occupancy costs, related overhead, information technology and other general corporate expenses of approximately \$0.3 million. Non-recurring costs consisted of approximately \$0.4 million in consulting fees and executive relocation costs of approximately \$0.2 million, partially offset by a decrease in litigation costs of approximately \$0.3 million. Consulting fees related to pricing and cost efficiency analysis.

General and administrative expenses increased by 7% to \$21.6 million in the six months ended June 30, 2018 from \$20.1 million in the comparable period in 2017. This variance was primarily attributable to increases in total compensation and related employee expenses of approximately \$1.1 million, in business services and outsourced labor of approximately \$0.6 million, and in allocated occupancy costs, related overhead, information technology and other general corporate expenses of approximately \$0.2 million. This was partially offset by a net decrease in non-recurring costs of approximately \$0.4 million. Non-recurring costs consisted of a decrease in litigation costs of approximately \$1.3 million, partially offset by \$0.4 million in consulting fees, executive recruitment costs of \$0.3 million and executive relocation costs of approximately \$0.2 million. Consulting fees related to pricing and cost efficiency analysis.

Product Development

Our product development expenses consist of compensation and related expenses for product development personnel as well as allocated occupancy costs and related overhead and outsourced labor and expenses for testing new versions of our software.

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
Product development	\$14,219	\$9,326	52 %	\$27,471	\$19,285	42 %
Percentage of total revenue	23 %	17 %		23 %	18 %	
Headcount (at period end):	367	296	24 %	367	296	24 %

Product development costs increased by 52% and 42% to \$14.2 million and \$27.5 million in the three and six months ended June 30, 2018 from \$9.3 million and \$19.3 million in the comparable periods in 2017. This variance was primarily attributable to increases in total compensation, outside labor, recruiting expense and associated costs for existing product development personnel of approximately \$4.0 million and \$6.4 million, respectively, and in depreciation expense and backup server facilities and allocated overhead related to costs of supporting our server and network infrastructure of approximately \$0.9 and \$1.8 million, respectively.

We continue to invest in new product development efforts to expand the capability of LiveEngage. We recognize that every brand is unique and employs an individualized and complex approach to managing their users. In accordance with ASC 350-40 - "Internal- Use Software", as new projects are initiated that provide functionality to the LiveEngage platform, the associated development and employee costs will be capitalized. Upon completion, the project costs will be depreciated over five years. In the three and six months ended June 30, 2018, \$2.4 million and \$5.1 million was

capitalized, respectively. In the three and six months ended June 30, 2017, \$2.3 million and \$4.0 was capitalized, respectively.

Restructuring Costs

Restructuring costs consist of reprioritizing and reallocating resources to focus on areas showing high growth potential.

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	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
Restructuring costs	\$1,906	\$2,076	(8)%	\$2,084	\$2,315	(10)%
Percentage of total revenue	3 %	4 %		2 %	2 %	

Restructuring costs incurred decreased by 8% and 10% to approximately \$1.9 million and \$2.1 million during the three and six months ended June 30, 2018, respectively, from \$2.1 million and \$2.3 million in the comparable periods in 2017. This variance was primarily attributable to wind-down costs of our legacy platform of \$1.8 million and \$1.9 million during three and six months ended 2017. This was partially offset by increases in severance costs of \$1.6 million and \$1.7 million during three and six months ended June 30, 2018 from the comparable periods in 2017.

Amortization of Purchased Intangibles

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
Amortization of purchased intangibles	\$424	\$470	(10)%	\$848	\$942	(10)%
Percentage of total revenues	1 %	1 %		1 %	1 %	

Amortization expense for purchased intangibles decreased by 10% to \$0.4 million and \$0.8 million in the three and six months ended June 30, 2018, respectively, from \$0.5 million and \$0.9 million in the comparable periods in 2017. This variance was primarily attributable to a decrease in amortization of CAO! and Synchronite intangible assets. This was partially offset by amortization of the 2018 Bot Central assets acquired.

Additional amortization expense in the amount of \$0.3 million and \$1.0 million in the three months ended June 30, 2018 and 2017, respectively, and \$0.6 million and \$1.9 million in the six months ended June 30, 2018 and 2017, respectively, is included in cost of revenue. The decrease is primarily attributable to the full amortization of Amadesa during the third quarter of 2017.

Other Income, net

Other income, net consists of interest income on cash and cash equivalents, investment income and financial (expense) income which is a result of currency rate fluctuations associated with exchange rate movement of the U.S. dollar against the New Israeli Shekel, British Pound, Euro, Australian Dollar and Japanese Yen.

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017	% Change	2018	2017	% Change
	(\$ in thousands)			(\$ in thousands)		
Other income (expense), net	\$31	\$(99)	(131)%	\$ 160		