

LIVEPERSON INC
Form 10-Q
November 07, 2013

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

FORM 10-Q

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

For the quarterly period ended September 30, 2013

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 ✓ 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 ✓ 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 ✓

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☐

(Do not check if a smaller reporting company)

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

On November 1, 2013, 54,133,593 shares of the registrant's common stock were outstanding.

LIVEPERSON, INC.
 September 30, 2013
 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 PROGRESS, 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)

	September 30, 2013 (Unaudited)	December 31, 2012 (Note 1)
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$77,379	\$103,339
Accounts receivable, net of allowance for doubtful accounts of \$708 as of September 30, 2013 and December 31, 2012, respectively	32,726	23,830
Prepaid expenses and other current assets	7,049	6,369
Deferred tax assets, net	4,031	2,616
Total current assets	121,185	136,154
Property and equipment, net	18,183	17,495
Intangibles, net	14,156	15,681
Goodwill	32,724	32,645
Deferred tax assets, net	4,755	4,183
Other assets	2,327	2,418
Total assets	\$193,330	\$208,576
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$9,209	\$11,125
Accrued expenses	20,347	17,911
Deferred revenue	6,779	6,525
Total current liabilities	36,335	35,561
Deferred revenue, net of current	1,270	1,263
Other liabilities	1,397	1,509
Total liabilities	39,002	38,333
Commitments and contingencies (See Note 10)		
STOCKHOLDERS' EQUITY (See Note 11):		
Common stock	54	56
Additional paid-in capital	239,227	252,320
Accumulated deficit	(84,571)	(81,780)
Accumulated other comprehensive loss	(382)	(353)
Total stockholders' equity	154,328	170,243
Total liabilities and stockholders' equity	\$193,330	\$208,576

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		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Revenue	\$45,192	\$39,670	\$130,917	\$114,934
Costs and expenses:				
Cost of revenue	10,597	9,036	31,342	25,450
Sales and marketing	16,141	12,713	46,118	36,820
Product development	10,023	8,005	27,091	21,881
General and administrative	9,508	7,316	29,581	22,784
Amortization of purchased intangibles	224	11	672	98
Total costs and expenses	46,493	37,081	134,804	107,033
(Loss) income from operations	(1,301	) 2,589	(3,887	) 7,901
Other income	209	41	264	155
(Loss) income before (benefit from) provision for income taxes	(1,092	) 2,630	(3,623	) 8,056
(Benefit from) provision for income taxes	(362	) 1,030	(832	) 3,193
Net (loss) income	\$(730	) \$1,600	\$(2,791	) \$4,863
Net (loss) income per share of common stock:				
Basic	\$(0.01	) \$0.03	\$(0.05	) \$0.09
Diluted	\$(0.01	) \$0.03	\$(0.05	) \$0.09
Weighted-average shares used to compute net (loss) income per share:				
Basic	54,046,161	55,688,824	54,898,974	55,087,109
Diluted	54,046,161	57,760,868	54,898,974	56,987,302

See Notes to Condensed Consolidated Financial Statements (unaudited).

LIVEPERSON, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME

(IN THOUSANDS)

(UNAUDITED)

	Three Months Ended		Nine Months Ended		
	September 30,		September 30,		
	2013	2012	2013	2012	
Net (loss) income	\$ (730	) \$ 1,600	\$ (2,791	) \$ 4,863
Foreign currency translation adjustment	358	(200) (29) (156)
Comprehensive (loss) income	\$ (372	) \$ 1,400	\$ (2,820	) \$ 4,707

See Notes to Condensed Consolidated Financial Statements (unaudited).

LIVEPERSON, INC.

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

	Nine Months Ended September 30,	
	2013	2012
OPERATING ACTIVITIES:		
Net (loss) income	\$(2,791	) \$4,863
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Stock-based compensation expense	9,749	7,646
Depreciation	6,050	5,170
Amortization of purchased intangibles	1,575	294
Deferred income taxes	(1,700	) (1,325
Provision for doubtful accounts, net	—	20
Changes in operating assets and liabilities:		
Accounts receivable	(7,395	) (1,846
Prepaid expenses and other current assets	(1,523	) (1,617
Other assets	79	(81
Accounts payable	(3,523	) 1,129
Accrued expenses	2,978	2,121
Deferred revenue	261	1,373
Other liabilities	(112	) (81
Net cash provided by operating activities	3,648	17,666
INVESTING ACTIVITIES:		
Purchases of property and equipment, including capitalized software	(6,638	) (6,919
Acquisition of LookIO, net of cash acquired	—	(900
Acquisition of Amadesa technology assets	—	(10,798
Acquisition of Proficient	—	(77
Acquisition of domains	(50) —
Acquisition costs - Engage, net of cash	(79) —
Net cash used in investing activities	(6,767	) (18,694
FINANCING ACTIVITIES:		
Excess tax benefit from the exercise of employee stock options	135	2,607
Proceeds from issuance of common stock in connection with the exercise of options	3,737	8,557
Repurchase of common stock	(26,716) —
Net cash (used in) provided by financing activities	(22,844	) 11,164
EFFECT OF FOREIGN EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	3	(130
CHANGE IN CASH AND CASH EQUIVALENTS	(25,960	) 10,006
CASH AND CASH EQUIVALENTS - Beginning of the period	103,339	93,278
CASH AND CASH EQUIVALENTS - End of the period	\$77,379	\$ 103,284

SUPPLEMENTAL DISCLOSURE OF OTHER CASH FLOW INFORMATION:

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Cash paid for income taxes	\$151	\$1,556
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SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:

Purchase of property and equipment recorded in accounts payable	\$720	\$1,952
Issuance of 109,517 shares of common stock in connection with the acquisition of LookIO on June 13, 2012	\$—	\$1,984

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 offices in Amsterdam, Atlanta, London, Melbourne, San Francisco, Santa Monica and Tel Aviv.

LivePerson provides online engagement solutions offering a cloud-based platform which enables businesses to proactively connect with consumers through chat, voice and content delivery, across multiple channels and screens, including websites, social media, and mobile devices. The Company’s engagements are driven by insights derived from a broad set of consumer and business data, including historical, behavioral, operational, and third party data. Each engagement is based on proprietary analytics and a real-time understanding of consumer needs and business objectives. The Company’s products, coupled with its domain knowledge and industry expertise, have been proven to maximize the effectiveness of the online channel — by increasing sales, as well as consumer satisfaction and loyalty ratings for their customers, while also enabling their customers to reduce consumer service costs.

LivePerson monitors and analyzes valuable online consumer behavioral data on behalf of its customers. Spanning the breadth of an online visitor session starting from an initial keyword search, through actions on their customer’s website, and even into a shopping cart and an executed sale, this data enables the Company to develop unique insights into consumer behavior during specific transactions within a customer’s user base.

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 September 30, 2013 and for the three and nine months ended September 30, 2013 and 2012 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 September 30, 2013, and the consolidated results of operations, comprehensive (loss) income and cash flows for the interim periods ended September 30, 2013 and 2012. 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, 2012 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, 2012, included in the Company’s Annual Report on Form 10-K filed with the SEC on March 1, 2013.

Reclassification

For comparability, certain 2012 amounts have been reclassified where appropriate, to conform to the financial presentation in 2013.

Principles of Consolidation

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

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

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Comprehensive Income

In February 2013, the FASB issued ASU No. 2013-2, Reporting of Amounts Reclassified out of Accumulated Other Comprehensive Income. This ASU requires disclosures regarding reclassifications out of accumulated other comprehensive income in a single location in the financial statements by component. This ASU is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2012. The adoption of this ASU, effective January 1, 2013, did not have an impact on the Company's condensed consolidated financial statements.

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. Because the Company provides its application as a service, the Company follows the provisions of Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 605-10-S99, "Revenue Recognition" and ASC 605-25, "Revenue Recognition with Multiple-Element Arrangements." The Company charges a monthly fee, which varies by type of service, the level of customer usage and website traffic, and in some cases, the number of orders placed via the Company's online engagement solutions.

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, the Company recognizes revenue net of the labor provider's fee in accordance with ASC 605-45, "Principal Agent Considerations," due primarily to the fact that the call center labor vendor is the primary obligor with respect to the labor services provided. Additionally, the Company performs as an agent without risk of loss for collection and does not bear inventory risk with respect to the outsourced labor services. Finally, the Company does not provide any part of the labor services, has no latitude in establishing prices for the labor services and generally does not have discretion in selecting the vendor.

The Company also sells certain of the LivePerson services directly via Internet download. These services are marketed as LivePerson Pro and LivePerson Contact Center for small and mid-sized businesses ("SMBs"), and are paid for almost exclusively by credit card. Credit card payments accelerate cash flow and reduce the Company's collection risk, subject to the merchant bank's right to hold back cash pending settlement of the transactions. Sales of LivePerson Pro and LivePerson Contact Center may occur with or without the assistance of an online sales representative, rather than through face-to-face or telephone contact that is typically required for traditional direct sales.

The Company recognizes monthly service revenue based upon the fee charged for the LivePerson services, provided that there is persuasive evidence of an arrangement, no significant Company obligations remain, collection of the resulting receivable is probable and the amount of fees to be paid is fixed or determinable. The Company's service agreements typically have twelve month terms and, in some cases, are terminable or may terminate upon 30 to 90 days' notice without penalty. When professional service fees add value to the customer on a standalone basis, the Company recognizes professional service fees upon completion and customer acceptance in accordance with FASB Accounting Standards Update 2009-13. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence; (b) third-party evidence; or (c) estimates. If a professional services arrangement does not qualify for separate accounting, the Company recognizes the fees, and the related labor costs, ratably over a period of 48 months, representing the Company's current estimate of the term of the customer relationship.

For revenue generated from online transactions between Experts and Users, the Company recognizes revenue net of the Expert fees in accordance with ASC 605-45, "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 User and retains a portion of the fee, and then remits the balance to the Expert. Revenue from these transactions is recognized when there is persuasive evidence of an arrangement, no significant Company obligations remain, collection of the resulting receivable is probable and the amount of fees to be paid is fixed and determinable.

3. Net Income (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 nine months ended September 30, 2013 does not include the effect of options to purchase 2,945,414 and 3,084,345, respectively, of common stock as the effect of their inclusion is anti-dilutive. Diluted net income per common share for the three and nine months ended September 30, 2012 includes the effect of options to purchase 5,413,038 and 5,015,988, respectively, shares of common stock with a weighted average exercise price of \$7.20 and \$6.82.

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

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Basic	54,046,161	55,688,824	54,898,974	55,087,109
Effect of assumed exercised options	—	2,072,044	—	1,900,193
Diluted	54,046,161	57,760,868	54,898,974	56,987,302

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 facilitates real-time online interactions – chat, voice and content delivery across multiple channels and screens for global corporations of all sizes. The Consumer segment facilitates online transactions between Experts and Users and sells its services to consumers. Both segments currently generate their revenue primarily in the U.S. The chief operating decision makers evaluate performance, make operating decisions, and allocate 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 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 September 30, 2013, based on the Company's internal financial reporting system utilized by the Company's chief operating decision makers, follows (amounts in thousands):

	Consolidated	Corporate	Business	Consumer
Revenue:				
Hosted services – Business	\$38,007	\$—	\$38,007	\$—
Hosted services – Consumer	3,828	—	—	3,828
Professional services	3,357	—	3,357	—
Total revenue	45,192	—	41,364	3,828
Cost of revenue	10,597	—	10,014	583
Sales and marketing	16,141	—	14,664	1,477
Amortization of purchased intangibles	224	—	224	—
Unallocated corporate expenses	19,531	19,531	—	—
Operating (loss) income	\$(1,301)	\$(19,531)	\$16,462	\$1,768

Summarized financial information by segment for the three months ended September 30, 2012, based on the Company's internal financial reporting system utilized by the Company's chief operating decision makers, follows (amounts in thousands):

	Consolidated	Corporate	Business	Consumer
Revenue:				
Hosted services – Business	\$33,245	\$—	\$33,245	\$—
Hosted services – Consumer	3,577	—	—	3,577
Professional services	2,848	—	2,848	—
Total revenue	39,670	—	36,093	3,577
Cost of revenue	9,036	—	8,539	497
Sales and marketing	12,713	—	11,502	1,211
Amortization of purchased intangibles	11	—	11	—
Unallocated corporate expenses	15,321	15,321	—	—
Operating income (loss)	\$2,589	\$(15,321)	\$16,041	\$1,869

Summarized financial information by segment for the nine months ended September 30, 2013, based on the Company's internal financial reporting system utilized by the Company's chief operating decision makers, follows (amounts in thousands):

	Consolidated	Corporate	Business	Consumer
Revenue:				
Hosted services – Business	\$110,785	\$—	\$110,785	\$—
Hosted services – Consumer	11,223	—	—	11,223
Professional services	8,909	—	8,909	—
Total revenue	130,917	—	119,694	11,223
Cost of revenue	31,342	—	29,524	1,818
Sales and marketing	46,118	—	42,113	4,005
Amortization of purchased intangibles	672	—	672	—
Unallocated corporate expenses	56,672	56,672	—	—
Operating (loss) income	\$(3,887)	\$(56,672)	\$47,385	\$5,400

Summarized financial information by segment for the nine months ended September 30, 2012, based on the Company's internal financial reporting system utilized by the Company's chief operating decision makers, follows (amounts in thousands):

	Consolidated	Corporate	Business	Consumer
Revenue:				
Hosted services – Business	\$96,634	\$—	\$96,634	\$—
Hosted services – Consumer	11,387	—	—	11,387
Professional services	6,913	—	6,913	—
Total revenue	114,934	—	103,547	11,387
Cost of revenue	25,450	—	23,845	1,605
Sales and marketing	36,820	—	32,616	4,204
Amortization of purchased intangibles	98	—	98	—
Unallocated corporate expenses	44,665	44,665	—	—
Operating income (loss)	\$7,901	\$(44,665)	\$46,988	\$5,578

Geographic Information

The Company is domiciled in the United States and has international operations in the United Kingdom, Australia, Latin America and Western Europe, particularly France and Germany. The following table presents the Company's revenues attributable to domestic and foreign operations for the periods presented (amounts in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
United States	\$30,879	\$29,531	\$91,397	\$86,909
United Kingdom	8,554	5,898	22,501	16,017
Other countries	5,759	4,241	17,019	12,008
Total revenue	\$45,192	\$39,670	\$130,917	\$114,934

The following table presents the Company's long-lived assets by geographic region for the periods presented (amounts in thousands):

	September 30,	December 31,
	2013	2012
United States	\$36,042	\$35,711
Israel	23,790	23,750
Australia	10,124	10,361
United Kingdom	1,633	2,600
Netherlands	556	—
Total long-lived assets	\$72,145	\$72,422

5. Goodwill and Intangible Assets

The changes in the carrying amount of goodwill for the nine months ended September 30, 2013 are as follows (amounts in thousands):

	Total	Business	Consumer
Balance as of December 31, 2012	\$32,645	\$24,621	\$8,024
Adjustments to goodwill:			
Engage acquisition (see Note 8)	79	79	—
Balance as of September 30, 2013	\$32,724	\$24,700	\$8,024

The changes in the carrying amount of goodwill for the year ended December 31, 2012 are as follows (amounts in thousands):

	Total	Business	Consumer
Balance as of December 31, 2011	\$24,090	\$16,066	\$8,024
Adjustments to goodwill:			
Engage acquisition	6,073	6,073	—
LookIO acquisition	2,405	2,405	—
Contingent earnout payments (see Note 8)	77	77	—
Balance as of December 31, 2012	\$32,645	\$24,621	\$8,024

Intangible assets are summarized as follows (see Note 8) (amounts in thousands):

Acquired Intangible Assets

As of September 30, 2013

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Amortization Period
Amortizing intangible assets:				
Technology	\$18,533	\$(6,808)	\$11,725	3.8 years
Customer relationships	5,061	(2,982)	2,079	3.5 years
Trade names	725	(716)	9	2.7 years
Non-compete agreements	486	(478)	8	1.2 years
Patents	475	(178)	297	11.0 years
Other	285	(247)	38	3.0 years
Total	\$25,565	\$(11,409)	\$14,156	

As of December 31, 2012

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Amortization Period
Amortizing intangible assets:				
Technology	\$18,533	\$(5,904)	\$12,629	3.8 years
Customer relationships	5,061	(2,485)	2,576	3.5 years
Trade names	725	(644)	81	2.7 years
Non-compete agreements	486	(421)	65	1.2 years
Patents	475	(145)	330	11.0 years
Other	235	(235)	—	3.0 years
Total	\$25,515	\$(9,834)	\$15,681	

Amortization expense is calculated on a straight-line basis over the estimated useful life of the asset. Aggregate amortization expense for intangible assets was \$0.7 million and \$1.6 million for the three and nine months ended September 30, 2013, respectively, and \$0.1 million and \$0.3 million for the three and nine months ended September 30, 2012, respectively. Estimated amortization expense for the next five years are as follows (amounts in thousands):

	Estimated Amortization Expense
2013	\$1,078
2014	4,133
2015	3,771
2016	3,316
2017	1,746
Thereafter	112
Total	\$14,156

6. Property and Equipment

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

	September 30, 2013	December 31, 2012
Computer equipment and software	\$44,412	\$38,649
Furniture, equipment and building improvements	7,809	6,834

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	52,221	45,483	
Less: accumulated depreciation	(34,038) (27,988)
Total	\$18,183	\$17,495	

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7. Accrued Liabilities

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

	September 30, 2013	December 31, 2012
Payroll and other employee related costs	\$10,768	\$9,199
Professional services and consulting and other vendor fees	6,151	5,698
Sales commissions	1,128	490
Contingent earnout (Note 8)	1,660	1,660
Other	640	864
Total	\$20,347	\$17,911

8. Acquisitions

Amadesa Ltd.

On May 31, 2012, the Company acquired technology assets from Amadesa, Ltd., an Israeli-based start-up, for aggregate cash consideration of approximately \$10.3 million. The acquisition provides the Company with sophisticated, machine-learning predictive modeling that it expects to leverage across multiple engagement channels, enhancing its real-time intelligent engagement platform. The asset is allocated to "Intangibles, net" on the Company's balance sheet and will be amortized over its expected period of benefit. The acquisition did not have a material impact on the Company's reported operating results. Total acquisition costs incurred were approximately \$0.5 million and are included in "Intangibles, net" on the Company's September 30, 2013 balance sheet.

LookIO

On June 13, 2012, the Company acquired LookIO, Inc., a start-up that provides mobile engagement solutions. The transaction was accounted for under the purchase method of accounting and, accordingly, the operating results of LookIO, Inc. were included in the Company's consolidated results of operations from the date of acquisition. The acquisition did not have a material impact on the Company's reported operating results.

The purchase price was approximately \$2.9 million, which included the issuance of 109,517 shares of the Company's common stock valued at approximately \$2.0 million, based on the quoted market price of the Company's common stock on the day of closing, and a cash payment of \$0.9 million. Total acquisition costs incurred were approximately \$0.2 million and were included in general and administrative expenses in the Company's consolidated statements of operations for the same period. The acquisition adds plug-and-play mobile engagement capabilities to LivePerson's platform allowing its customers to connect with consumers on mobile devices. All 109,517 shares are included in the weighted average shares outstanding used in basic and diluted net income (loss) per share as of the acquisition date.

The purchase price was allocated based on management's estimate of fair values, taking into account all relevant information available. A substantial amount of the purchase price was allocated to intangibles (technology) and the excess was allocated to goodwill. The goodwill is not deductible for income tax purposes. The intangible asset is being amortized over its expected period of benefit. In addition to the purchase price, certain founders can earn an additional 30,422 shares of LivePerson common stock by achieving an employment milestone by providing continued services through a specified date. The Company valued these shares at approximately \$0.6 million, based on the quoted market price of the Company's common stock on the day of closing. In accordance with ASC 805-10, the Company is accruing this contingent compensation ratably over the requisite employment period.

Management's allocation of the purchase price in connection with the LookIO acquisition is as follows (amounts in thousands):

Intangible assets (technology)	\$767	
Goodwill	2,405	
	3,172	
Deferred tax liability	(288)
Total purchase price consideration	\$2,884	

Engage Pty Ltd.

On November 9, 2012, the Company acquired all outstanding shares of Engage Pty Ltd. ("Engage"), an Australian provider of cloud-based customer contact solutions. The transaction was accounted for under the purchase method of

accounting and,

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accordingly, the operating results of Engage were included in the Company's consolidated results of operations from the date of acquisition. The acquisition did not have a material impact on the Company's reported operating results. The purchase price was approximately \$10.6 million. The total acquisition costs incurred in the year ended December 31, 2012 were approximately \$0.5 million and are included in general and administrative expenses in the Company's consolidated statements of operations for the same period. The acquisition enhances the Company's ability to offer intelligent engagement solutions to businesses in the Asia Pacific region. Of the total purchase price, \$0.8 million was allocated to the net book values of the acquired assets and assumed liabilities. The historical carrying amounts of such assets and liabilities approximated their fair values. All receivables acquired are expected to be collectible. The purchase price in excess of the fair value of the net book values of the assets acquired and liabilities assumed was allocated to intangible assets based on management's best estimate of fair values, taking into account all relevant information available at the time of acquisition, and the excess was allocated to goodwill. The goodwill is not deductible for tax purposes. The intangible assets are being amortized over their expected period of benefit. The purchase price includes approximately \$1.7 million of potential earn-out consideration for the shareholders if certain revenue targets are achieved. The earn-out is payable in shares of LivePerson common stock. The Company recorded the contingent earn-out as part of the purchase price. In accordance with ASC 480, the Company has classified this amount as a liability and the amount is included in the September 30, 2013 balance sheet, due to the variable number of shares that will be issued if and when the targets are achieved. The Company will assess the earn-out calculation in future periods and any future adjustments will affect operating income. During the nine months ended September 30, 2013, the Company incurred an additional net working capital adjustment of \$79,000. This amount has been included as part of the purchase price consideration resulting in an increase in goodwill.

Management's preliminary allocation of the purchase price in connection with the Engage acquisition is as follows (amounts in thousands):

Cash	\$386	
Accounts receivable	3,454	
Other current assets	57	
Property and equipment	432	
Other assets	104	
Intangible assets	3,600	
Goodwill	6,152	
	14,185	
Liabilities assumed	(2,632)
Deferred tax liability	(962)
Total purchase price consideration	\$10,591	

The components of the intangible assets listed in the above table are as follows (amounts in thousands):

	Weighted Average Useful Life (Months)	Amount
Technology	36	\$768
Trade-name	12	95
Customer relationships	48	2,661
Non-compete agreements	12	76
		\$3,600

9. 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.

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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.

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 September 30, 2013 and December 31, 2012, are summarized as follows (amounts in thousands):

	September 30, 2013				December 31, 2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets:								
Cash equivalents:								
Money market funds	\$19,168	\$—	\$—	\$19,168	\$20,745	\$—	\$—	\$20,745
Total assets	\$19,168	\$—	\$—	\$19,168	\$20,745	\$—	\$—	\$20,745

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 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 only asset or liability that is measured at fair value on a recurring basis is money market funds, based on quoted market prices in active markets and therefore classified as level 1 within the fair value hierarchy. The carrying value of cash and cash equivalents, accounts receivable, accounts payable and certain accrued expenses approximate fair value because of their short-term maturity. 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 a combination of discounted cash flows and other 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.

10. 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 and nine months ended September 30, 2013 was approximately \$2.2 million and \$6.9 million, respectively. Rental expense for operating leases for the three and nine months ended September 30, 2012 was approximately \$2.0 million and \$5.3 million, respectively.

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 \$0.2 million and \$0.7 million of employer matching contributions for the three and nine months ended September 30, 2013, respectively. Salaries and related expenses include \$0.2 million and \$0.5 million of employer matching contributions for the three and nine months ended September 30, 2012, respectively.

11. Stockholders' Equity

Common Stock

As of September 30, 2013, the Company had 54,123,328 common shares issued and outstanding. As of December 31, 2012, the Company had 55,948,924 shares issued and outstanding. The par value for common shares was \$0.001.

Preferred Stock

As of September 30, 2013 and December 31, 2012, the Company had zero preferred shares issued and outstanding. The par value for preferred shares was \$0.001.

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 following table summarizes stock-based compensation expense related to employee stock options under ASC 718-10 included in Company's Statements of Operations for the three and nine months ended September 30, 2013 and 2012 (amounts in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Cost of revenue	\$635	\$428	\$1,557	\$1,130
Sales and marketing expense	844	822	2,159	2,113
Product development expense	1,241	807	2,922	2,206
General and administrative expense	1,078	795	3,111	2,197
Total stock based compensation included in costs and expenses	\$3,798	\$2,852	\$9,749	\$7,646

The per share weighted average fair value of stock options granted during the three and nine months ended September 30, 2013 was \$4.82 and \$5.25, respectively. The per share weighted average fair value of stock options granted during the three and nine months ended September 30, 2012 was \$8.78 and \$8.23, 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		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Dividend yield	0.0	% 0.0	% 0.0	% 0.0
Risk-free interest rate	1.38% - 1.39%	0.58% - 0.62%	0.65% - 1.39%	0.58% - 0.87%
Expected life (in years)	5	5	5	5
Historical volatility	59.84% - 59.85%	59.7% - 60.3%	56.68% - 60.06%	59.7% - 60.8%

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.

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 to purchase 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 stock incentive plan (the “Amended 2009 Plan”) effective June 7, 2012. The Amended 2009 Plan increased the number

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of shares authorized for issuance under the plan by an additional 4,250,000, thereby reserving for issuance 23,817,744 shares of common stock in the aggregate. Options to acquire common stock granted thereunder have ten-year terms. As of September 30, 2013, approximately 15,000,000 shares of common stock were reserved for issuance under the 2009 Plan (taking into account all option exercises through September 30, 2013). As of September 30, 2013, there was approximately \$33.4 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 2.0 years.

In March 2000, the Company adopted the 2000 Employee Stock Purchase Plan with 450,000 shares of common stock initially reserved for issuance (the "2000 ESPP"). The 2000 ESPP expired on its terms on the last day of April 2010. In June 2010, our stockholders approved the 2010 Employee Stock Purchase Plan with 1,000,000 shares of common stock initially reserved for issuance. As of September 30, 2013, approximately 726,000 shares of common stock were reserved for issuance under the Employee Stock Purchase Plan (taking into account all share purchases through September 30, 2013).

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

	Options	Weighted Average Exercise Price
Options outstanding at December 31, 2012	9,841,479	\$11.06
Options granted	2,121,200	10.38
Options exercised	(446,107)	5.94
Options cancelled	(1,384,530)	13.05
Options outstanding at September 30, 2013	10,132,042	10.87
Options exercisable at September 30, 2013	4,451,913	\$8.54

The total value of stock options exercised during the nine months ended September 30, 2013 was approximately \$2.1 million. The total intrinsic value of options exercisable at September 30, 2013 was approximately \$11.9 million. The total intrinsic value of nonvested options at September 30, 2013 is approximately \$0.5 million. The total intrinsic value of all outstanding options at September 30, 2013 is \$12.5 million.

A summary of the status of the Company's nonvested shares as of December 31, 2012, and changes during the nine months ended September 30, 2013 is as follows:

	Options	Weighted Average Grant- Date Fair Value
Nonvested Shares at December 31, 2012	6,621,251	\$ 6.84
Granted	2,121,200	5.25
Vested	(1,677,792)	6.03
Cancelled	(1,384,530)	6.72
Nonvested Shares at September 30, 2013	5,680,129	\$ 6.90

12. Legal Matters

On February 7, 2012, the Company filed suit against Pragmatius Telecom LLC in the District of Delaware, seeking a declaratory judgment that the Company's products do not infringe three patents owned by Pragmatius which Pragmatius had previously asserted were infringed by certain of the Company's customers. On March 13, 2012, the Company amended the complaint to add a request for a declaratory judgment that those three patents are invalid. On April 6, 2012, Pragmatius answered the Amended Complaint, and asserted counterclaims against the Company asserting infringement of the same three patents and seeking unspecified monetary damages and injunctive relief. The Court entered a Scheduling Order on June 1, 2012 scheduling trial in this matter to begin on or after September 8, 2014. The matter is presently stayed until December 2013. The Company currently does not expect that the outcome of this matter will have a material adverse effect on the Company's financial condition, results of operations or cash flows. However, litigation is inherently unpredictable; therefore, judgments could be rendered or settlements entered, that could adversely affect the Company's operating results or cash flows in a particular period. Though it is reasonably

possible that the Company will incur a liability associated with this litigation, the amount of any such liability is not reasonably estimable at this time.

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 it 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 its customers for whom it 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 disclosures 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.

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 are 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, 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 provides online engagement solutions offering a cloud-based platform which enables businesses to pro-actively connect with consumers and an online marketplace providing information and knowledge. We are organized into two operating segments: Business and Consumer. The Business segment facilitates real-time online interactions — chat, voice and content delivery, across multiple channels and screens for global corporations of all sizes. The Consumer segment facilitates online transactions between independent service providers (“Experts”) and individual consumers (“Users”) seeking information and knowledge for a fee via real-time chat. We were incorporated in the State of Delaware in November 1995 and the LivePerson service was introduced initially in November 1998.

In order to sustain growth in these segments, our strategy is to expand our position as the leading provider of online engagement solutions that facilitate real-time assistance and expert advice. To accomplish this, we are focused on the following current initiatives:

Expanding Business with Existing Customers and Adding New Customers. We are expanding our sales capacity by adding enterprise and midmarket sales agents. We have also expanded our efforts to retain existing SMB customers through increased interaction with them during the early stages of their usage of our services.

Introducing New Products and Capabilities. We are investing in product marketing, research and development and executive personnel to support our expanding efforts to build and launch new products and capabilities to support existing customer deployments, and to further penetrate our total addressable market. These investments are initially focused in the areas of online marketing engagement and chat transcript text analysis. Over time, we expect to develop and launch additional capabilities that leverage our existing market position as a leader in proactive, intelligence-driven online engagement.

Expanding our international presence. We continue to increase our investment in sales and support personnel in the United Kingdom, Australia, Latin America and Western Europe, particularly France and Germany. We are also working with sales and support partners as we expand our investment in the Asia-Pacific region. We continue to improve the multi-language and translation capabilities within our hosted solutions to further support international expansion.

Third Quarter 2013

Financial overview of the three months ended September 30, 2013 compared to the three months ended September 30, 2012:

Total revenue increased 14% to \$45.2 million from \$39.7 million.

Revenue from our Business segment increased 15% to \$41.4 million from \$36.1 million.

Gross profit margin remained flat at 77%.

Operating expenses increased 25% to \$46.5 million from \$37.1 million.

Net income decreased to a net loss of \$0.7 million from net income of \$1.6 million.

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Bookings increased 26% and 17% to \$10.2 million and \$24.7 million in the three and nine months ended September 30, 2013, respectively, from \$8.1 million and \$21.1 million in the comparable periods in 2012. We include in our bookings metrics new contractual commitments from either new or existing

midmarket and/or enterprise customers for recurring subscription based fees, but exclude from such amounts non-recurring fees such as one time implementation costs or one time consulting fees. The bookings metric generally does not include or represent usage based and/or pay-for-performance based contracts, month-to-month contracts or transaction-based services. Accordingly, while we believe that bookings is a relevant metric in providing management with insight into certain recent activity in our business, there is no assurance that bookings amounts will be recognized as revenue in future periods, based on our revenue recognition policy, potential customer cancelations, delays in implementations or otherwise.

Average deal size for new bookings in the three and nine months ended September 30, 2013 was \$62,300 and \$54,800, respectively, with average deal size for new customers of \$53,300 and \$50,900, respectively, and average deal size for existing customers requesting additional products or expanded access to current products of \$66,900 and \$56,500, respectively. Average deal size for new bookings in the three and nine months ended September 30, 2012 was \$43,900 and \$48,200, respectively, with average deal size for new customers of \$50,800 and \$42,600, respectively, and average deal size for existing customers requesting additional products or expanded access to current products of \$41,200 and \$50,200, respectively. Similar to our bookings metric, average deal size generally represents new contractual arrangements with committed subscription or base fees from new or existing mid-market or enterprise customers, and does not capture usage and/or pay-for-performance based contracts or fees. Management uses average deal size, being a subset of bookings, as a relevant metric in providing management with insight into certain recent activity in our business.

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) income, 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 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		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Reconciliation of Adjusted EBITDA				
Net (loss) income	\$(730	) \$1,600	\$(2,791	) \$4,863
Amortization of purchased intangibles	691	140	1,575	294
Stock-based compensation	3,798	2,852	9,749	7,646
Depreciation	2,002	1,841	6,050	5,170
(Benefit from) provision for income taxes	(362	) 1,030	(832	) 3,193
Other (income)	(209	) (41	) (264	) (155
Adjusted EBITDA	\$5,190	\$7,422	\$13,487	\$21,011

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 are non-cash charges, 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;
- 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 income (loss) and our other GAAP results. The following table presents a reconciliation of adjusted net income for each of the periods indicated (amounts in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Reconciliation of Adjusted Net Income				
Net (loss) income	\$(730	) \$1,600	\$(2,791	) \$4,863
Amortization of purchased intangibles	691	140	1,575	294
Stock-based compensation	3,798	2,852	9,749	7,646
Adjusted net income	\$3,759	\$4,592	\$8,533	\$12,803

Critical Accounting Policies and Estimates

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 our revenue is generated from monthly service revenues and related professional services from the sale of the LivePerson services. Because we provide our application as a service, we follow the provisions of ASC 605-10-S99, "Revenue Recognition" and ASC 605-25, "Revenue Recognition with Multiple-Element Arrangements." We charge a monthly fee, which varies by type of service, the level of customer usage and website traffic, and in some cases, the number of orders placed via our online engagement solutions.

For certain of 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 our 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, we recognize revenue net of the labor provider's fee in accordance with ASC 605-45, "Principal Agent Considerations," due primarily to the fact that the call center labor vendor is the primary obligor with respect to the labor services provided. Additionally, we perform as an agent without risk of loss for collection and do not bear inventory risk with

respect to the outsourced labor services. Finally, we do not provide any part of the labor services, have no latitude in establishing prices for the labor services and generally do not have discretion in selecting the vendor.

We also sell certain of the LivePerson services directly via Internet download. These services are marketed as LivePerson Pro and LivePerson Contact Center for small and mid-sized businesses (“SMBs”), and are paid for almost exclusively by credit card. Credit card payments accelerate cash flow and reduce our collection risk, subject to the merchant bank’s right to hold back cash pending settlement of the transactions. Sales of LivePerson Pro and LivePerson Contact Center may occur with or without the assistance of an online sales representative, rather than through face-to-face or telephone contact that is typically required for traditional direct sales.

We recognize monthly service revenue based upon the fee charged for the LivePerson services, provided that there is persuasive evidence of an arrangement, no significant Company obligations remain, collection of the resulting receivable is probable and the amount of fees to be paid is fixed or determinable. Our service agreements typically have twelve month terms and are terminable or may terminate upon 30 to 90 days’ notice without penalty. When professional service fees add value to the customer on a standalone basis, we recognize professional service fees upon completion and customer acceptance in accordance with FASB Accounting Standards Update 2009-13. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence; (b) third-party evidence; or (c) estimates. If a professional services arrangement does not qualify for separate accounting, we recognize the fees, and the related labor costs, ratably over a period of 48 months, representing our current estimate of the term of the customer relationship.

For revenue generated from online transactions between Experts and Users, we recognize revenue net of Expert fees in accordance with ASC 605-45, “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 retain a portion of the fee, and then remit the balance to the Expert. Revenue from these transactions is recognized when there is persuasive evidence of an arrangement, no significant Company obligations remain, collection of the resulting receivable is probable and the amount of fees to be paid is fixed or determinable.

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 September 30, 2013, there was approximately \$33.4 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 2.0 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 nine months ended September 30, 2013. One customer accounted for approximately 16% and 15% of accounts receivable as of September 30, 2013 and December 31, 2012, respectively. There was no change in our allowance for doubtful accounts in the three months ended September 30, 2013.

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, the 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) than 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 analyses 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 comparables.

In the third quarter of 2013, 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. In July 2012, the FASB issued ASU No. 2012-02, Intangibles-Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment. This ASU states that an entity has the option first to assess qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not that the indefinite-lived intangible asset is impaired. If, after assessing the totality of events and circumstances, an entity concludes that it is not more likely than not that the indefinite-lived intangible asset is impaired, then the entity is not required to take further action. However, if an entity concludes otherwise, then it is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment test by comparing the fair value with the carrying amount in accordance with Codification Subtopic 350-30, Intangibles-Goodwill and Other, General Intangibles Other than Goodwill. Recoverability of assets to be held and used is measured by a comparison of the carrying value of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying value of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying value of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying value or the fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

Use of Estimates

The preparation of our consolidated financial statements in accordance with accounting principles generally accepted in the U.S. requires our management to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the period. Significant items subject to such estimates and assumptions include the carrying amount of goodwill, intangibles, stock-based compensation, valuation allowances for deferred income tax assets, accounts receivable, the expected term of a customer relationship, accruals and other factors. Actual results could differ from those estimates.

Recently Issued Accounting Standards

In February 2013, the FASB issued ASU No. 2013-02, Reporting of Amounts Reclassified out of Accumulated Other Comprehensive Income (Loss). This ASU requires disclosures regarding reclassifications out of accumulated other comprehensive income in a single location in the financial statements by component. This ASU is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2012. The adoption of this ASU, effective January 1, 2013, did not have an impact on our condensed consolidated financial statements.

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 fee, which varies by service and customer usage. The majority of our larger customers also pay a professional services fee related to implementation. 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.

Revenue from our Business segment accounted for 92% and 91% of total revenue for the three and nine months ended September 30, 2013, respectively. Revenue attributable to our monthly hosted Business services accounted for 92% and 93% of total Business revenue for the three and nine months ended September 30, 2013, respectively. Revenue from our Business

segment accounted for 91% and 90% of total revenue for the three and nine months ended September 30, 2012, respectively. Revenue attributable to our monthly hosted Business services accounted for 92% and 93% of total Business revenue for the three and nine months ended September 30, 2012, respectively. 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 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% and 9% of total revenue for the three and nine months ended September 30, 2013, respectively. Revenue generated from online transactions between Experts and Users accounted for approximately 9% and 10% of total revenue in each of the three and nine months ended September 30, 2012, respectively.

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;
- compensation costs relating to our network support staff;
- depreciation of certain hardware and software;
- 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 the consumer and SMB services; and
- amortization of certain intangibles.

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.

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, 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 and human resources personnel, allocated occupancy costs and related overhead, professional fees, provision for doubtful accounts and other general corporate expenses.

During the nine months ended September 30, 2013, we did not increase our allowance for doubtful accounts. During 2012, we increased our allowance for doubtful accounts by \$20,000 to approximately \$0.7 million, principally due to an increase in accounts receivable as a result of increased sales and, to a lesser extent, to an increase in the proportion of receivables due from customers with greater credit risk. A larger proportion of 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. We adjust our allowance for doubtful accounts when accounts previously reserved have been collected.

Non-Cash Compensation Expense

The net non-cash compensation amounts for the three and nine months ended September 30, 2013 and 2012 consist of:

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2013	
	2012	(in thousands)	2012	(in thousands)
Stock-based compensation expense related to ASC 718-10	\$3,798	\$2,852	\$9,749	\$7,646

Results of Operations

The Company is organized into two operating segments: Business and Consumer. The Business segment facilitates real-time online interactions — chat, voice and content delivery, across multiple channels and screens for global corporations of all sizes. The Consumer segment facilitates online transactions between Experts and Users seeking information and knowledge for a fee via real-time chat.

Comparison of Three and Nine Months Ended September 30, 2013 and 2012

Revenue

	Three Months Ended September 30, 2013			Nine Months Ended September 30, 2013		
	2012	% Change	(in thousands)	2012	% Change	(in thousands)
Revenue by Segment:						
Business	\$41,364	15 %	\$36,093	\$119,694	16 %	\$103,547
Consumer	3,828	7 %	3,577	11,223	(1) %	11,387
Total	\$45,192	14 %	\$39,670	\$130,917	14 %	\$114,934

Business revenue increased by 15% and 16% to \$41.4 million and \$119.7 million in the three and nine months ended September 30, 2013, respectively, from \$36.1 million and \$103.5 million in the comparable periods in 2012. This increase is primarily attributable to increased revenue from existing customers who increased their use of our services in the amount of approximately \$3.5 million and \$12.6 million, respectively, net of cancellations; revenue from new customers in the amount of approximately \$1.4 million and \$1.5 million, respectively; and, to a lesser extent, to professional services revenue of approximately \$0.3 million and \$1.8 million, respectively. Our revenue growth has traditionally been driven by a mix of revenue from new customers as well as expansion from existing customers.

Consumer revenue increased by 7% to \$3.8 million in the three months ended September 30, 2013, from \$3.6 million in the comparable period in 2012. This increase is primarily attributable to a increase in gross revenue as a result of an increase in the price charged per minute partially offset by an decrease in chat minutes. Consumer revenue decreased by 1% to \$11.2 million in the nine months ended September 30, 2013, from \$11.4 million in the comparable period in 2012. This decrease is primarily attributable to a decrease in gross revenue as a result of decreased chat minutes partially offset by an increase in the price charged per minute.

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, the cost of supporting our server and network infrastructure, and allocated occupancy costs and related overhead.

	Three Months Ended September 30, 2013			Nine Months Ended September 30, 2013		
	2012	% Change	(\$ in thousands)	2012	% Change	(\$ in thousands)
Cost of revenue - business	\$10,014	17 %	\$8,539	\$29,524	24 %	\$23,845
Percentage of total revenue	22 %			23 %		21 %
Headcount (at period end):	183	7 %	171	183	7 %	171

Cost of revenue increased by 17% to \$10.0 million in the three months ended September 30, 2013, from \$8.5 million in the comparable period in 2012. This increase in expense is primarily attributable to an increase in total compensation and related costs for additional and existing customer service and network operations personnel in the amount of approximately \$1.4 million. Cost of revenue increased by 24% to \$29.5 million in the nine months ended

September 30, 2013, from \$23.8 million in the

comparable period in 2012. This increase in expense is primarily attributable to an increase in total compensation and related costs for additional and existing customer service and network operations personnel in the amount of approximately \$4.3 million, and an increase in expense for primary and backup server facilities and allocated overhead related to costs of supporting our server and network infrastructure of approximately \$0.4 million, as a result of increased revenue and an increase in amortization of intangibles of approximately \$0.8 million, as a result of our acquisitions of Amadesa, LookIO and Engage Pty Ltd. This increase in cost of revenue was driven primarily by increased investment in more robust business continuity capabilities within our hosting facilities. In addition, costs related to data collection and storage have increased, as we have improved the scope and quality of the analytical reporting we provide to our larger customers.

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 September 30,			Nine Months Ended September 30,				
	2013	2012	% Change	2013	2012	% Change		
	(\$ in thousands)			(\$ in thousands)				
Cost of revenue - consumer	\$583	\$497	17 %	\$1,818	\$1,605	13 %		
Percentage of total revenue	1	% 1	%	1	% 1	%		
Headcount (at period end)	16	17	(6) %	16	17	(6) %		

Cost of revenue increased by 17% and 13% to \$0.6 million and \$1.8 million in the three and nine months ended September 30, 2013, respectively, from \$0.5 million and \$1.6 million in the comparable periods in 2012. This increase in expense is primarily attributable to an increase in total compensation and related costs for existing customer service personnel in the amount of approximately \$58,000 and \$0.2 million, respectively.

Product Development

Our product development expenses consist primarily 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 September 30,			Nine Months Ended September 30,				
	2013	2012	% Change	2013	2012	% Change		
	(\$ in thousands)			(\$ in thousands)				
Product development	\$10,023	\$8,005	25 %	\$27,091	\$21,881	24 %		
Percentage of total revenue	22	% 20	%	21	% 19	%		
Headcount (at period end):	214	212	1 %	214	212	1 %		

Product development costs increased by 25% and 24% to \$10.0 million and \$27.1 million in the three and nine months ended September 30, 2013, respectively, from \$8.0 million and \$21.9 million in the comparable periods in 2012. This increase is primarily attributable to an increase in compensation and related costs for additional and existing product development personnel as a result of our increased efforts to expand our product offerings of approximately \$1.6 million and \$4.3 million, respectively, as well as an increase in outsourced labor expense of approximately \$0.5 million and \$0.8 million, respectively, as a result of testing new versions of our software. We are increasing our investment in new product development efforts to expand future product offerings. We are also investing in partner programs that enable third-parties to develop value-added software applications for our existing and future customers.

Sales and Marketing - Business

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

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	% Change	2013	2012	% Change
	(\$ in thousands)			(\$ in thousands)		
Sales and marketing - business	\$14,664	\$11,502	27 %	\$42,113	\$32,617	29 %
Percentage of total revenue	32	% 29	%	32	% 28	%
Headcount (at period end):	250	208	20 %	250	208	20 %

Sales and marketing expenses increased by 27% to \$14.7 million in the three months ended September 30, 2013, from \$11.5 million in the comparable period in 2012. This increase is primarily attributable to an increase in compensation and related costs for additional and existing sales and marketing personnel of approximately \$3.1 million. Sales and marketing expenses increased by 29% to \$42.1 million in the nine months ended September 30, 2013, from \$32.6 million in the comparable period in 2012. This increase is primarily attributable to an increase in compensation and related costs for additional and existing sales and marketing personnel of approximately \$8.6 million and, to a lesser extent, an increase in advertising, public relations and trade show exhibit expenses of approximately \$0.5 million. This increase relates to our continued efforts to enhance our brand recognition and increase sales lead activity.

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 September 30,			Nine Months Ended September 30,		
	2013	2012	% Change	2013	2012	% Change
	(\$ in thousands)			(\$ in thousands)		
Sales and marketing - consumer	\$1,477	\$1,211	22 %	\$4,005	\$4,203	(5) %
Percentage of total revenue	3	% 3	%	3	% 4	%
Headcount (at period end):	5	4	25 %	5	4	25 %

Sales and marketing expenses increased by 22% to \$1.5 million in the three months ended September 30, 2013, from \$1.2 million in the comparable period in 2012. This increase is primarily attributable to an increase in advertising and online expenses of approximately \$0.2 million. Sales and marketing expenses decreased by 5% to \$4.0 million in the nine months ended September 30, 2013, from \$4.2 million in the comparable period in 2012. This decrease is primarily attributable to a decrease in compensation and related costs of marketing personnel of approximately \$0.4 million, as a result of realigning the responsibilities of certain employees to the Business segment partially offset by an increase in advertising expense of approximately \$0.2 million.

General and Administrative

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

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	% Change	2013	2012	% Change
	(\$ in thousands)			(\$ in thousands)		
General and administrative	\$9,508	\$7,316	30 %	\$29,581	\$22,784	30 %
Percentage of total revenue	21	% 18	%	23	% 20	%
Headcount (at period end):	83	71	17 %	83	71	17 %

General and administrative expenses increased by 30% to \$9.5 million in the three months ended September 30, 2013, from \$7.3 million in the comparable period in 2012. This increase is primarily attributable to an increase in compensation and related expenses for additional and existing accounting, legal, human resource and administrative

personnel in the amount of approximately \$1.3 million, an increase in professional fees of approximately \$0.4 million, an increase in rent expenses of approximately \$0.3 million and an increase in depreciation of approximately \$0.2 million. General and administrative expenses increased by 30% to \$29.6 million in the nine months ended September 30, 2013, from \$22.8 million in the comparable period in 2012. This increase is primarily attributable to an increase in compensation and related expenses for additional and existing

accounting, legal, human resource and administrative personnel in the amount of approximately \$3.8 million, an increase in accounting, legal and other professional fees of approximately \$1.1 million, an increase in rent expense of approximately \$1.0 million and an increase in depreciation of approximately \$0.6 million.

Amortization of Purchased Intangibles

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	% Change	2013	2012	% Change
	(\$ in thousands)			(\$ in thousands)		
Amortization of purchased intangibles	\$224	\$11	1,936 %	\$672	\$98	586 %
Percentage of total revenues	—	%	— %	1	%	— %

Amortization expense for purchased intangibles was \$0.2 million and \$0.7 million in the three and nine months ended September 30, 2013, respectively, and relates primarily to acquisition costs recorded as a result of our acquisitions of Engage in November 2012, LookIO in June 2012, Amadesa in May 2012, NuConomy in April 2010 and the purchases of patents in August 2009. Amortization expense was \$11,000 and \$98,000 in the three and nine months ended September 30, 2012, respectively, and relates primarily to acquisition costs recorded as a result of our acquisition of NuConomy in April 2010 and the purchase of patents in August 2009. The increase is attributable to the acquisition costs recorded as a result of our acquisitions in 2012. Additional amortization expense in the amount of \$0.5 million and \$0.9 million is included in cost of revenue for the three and nine months ended September 30, 2013, respectively. Amortization expense is expected to be approximately \$3.0 million in the year ended December 31, 2013.

Other Income

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	% Change	2013	2012	% Change
	(\$ in thousands)			(\$ in thousands)		
Other Income	\$209	\$41	410 %	\$264	\$155	70 %

Financial income was \$0.2 million in the three and nine months ended September 30, 2013, respectively, compared to \$22,000 and \$99,000 for the three and nine months ended September 30, 2012, respectively. Financial income is the result of currency rate fluctuations primarily associated with the exchange rate movement of the U.S. dollar against the New Israeli Shekel. Interest income was \$9,000 and \$33,000 in the three and nine months ended September 30, 2013, respectively, compared to \$19,000 and \$56,000 in the three and nine months ended September 30, 2012, respectively, and consists of interest earned on cash and cash equivalents.

(Benefit From) Provision for Income Taxes

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	% Change	2013	2012	% Change
	(\$ in thousands)			(\$ in thousands)		
(Benefit From) Provision for Income Taxes	\$(362)	\$1,030	(135)%	\$(832)	\$3,193	(126)%

Our effective tax rate was 33.2% and 23.0% for the three and nine months ended September 30, 2013, resulting in a benefit from income taxes of \$0.4 million and \$0.8 million, respectively. Our effective tax rate was 39.2% and 39.6% for the three and nine months ended September 30, 2012, respectively, resulting in a provision for income taxes of \$1.0 million and \$3.2 million in the three and nine months ended September 30, 2012, respectively.

Net (Loss) Income

We had net loss of \$0.7 million and \$2.8 million for the three and nine months ended September 30, 2013, respectively, and net income of \$1.6 million and \$4.9 million in the three and nine months ended September 30, 2012, respectively. Revenue increased by approximately \$5.5 million and \$16.0 million, respectively, while costs and expenses increased by approximately \$9.2 million and \$27.6 million, respectively. Other income increased approximately \$0.2 million and \$0.1 million for the three and nine months ended September 30, 2013, respectively. Income taxes decreased approximately \$1.3 million and \$4.0 million, contributing to a net decrease in net income of

approximately \$2.2 million and \$7.5 million for the three and nine months ended September 30, 2013, respectively.

Liquidity and Capital Resources

	Nine Months Ended September 30,	
	2013	2012
	(in thousands)	
Consolidated Statements of Cash Flows Data:		
Cash flows provided by operating activities	3,648	17,666
Cash flows used in investing activities	(6,767	) (18,694
Cash flows (used in) provided by financing activities	(22,844	) 11,164

As of September 30, 2013, we had approximately \$77.4 million in cash and cash equivalents, a decrease of approximately \$26.0 million from December 31, 2012. This decrease is primarily attributable to cash used to repurchase our common stock and net cash used in investing activities relating to purchases of fixed assets related to the build-out of our co-location facility. This is partially offset by proceeds from the issuance of common stock in connection with the exercise of stock options by employees and net cash provided by operating activities. We invest our cash in short-term money market funds.

Net cash provided by operating activities was \$3.6 million for the nine months ended September 30, 2013 and consisted primarily of non-cash expenses related to ASC 718-10, amortization of purchased intangibles and depreciation and an increase in accrued expenses, partially offset by a net loss, a decrease in accounts payable, and an increase in accounts receivable and prepaid expenses. Net cash provided by operating activities was \$17.7 million for the nine months ended September 30, 2012 and consisted primarily of net income, non-cash expenses related to ASC 718-10, amortization of intangibles and depreciation, increases in accounts payable, accrued expenses and deferred revenue partially offset by an increase in accounts receivable and prepaid expenses.

Net cash used in investing activities was \$6.8 million in the nine months ended September 30, 2013, and was due primarily to the purchase of fixed assets for our co-location facilities. Net cash used in investing activities was \$18.7 million in the nine months ended September 30, 2012, and was due primarily to our purchase of technology assets from Amadesa, our acquisition of LookIO, and the purchase of fixed assets for our co-location facilities.

Net cash used in financing activities was \$22.8 million in the nine months ended September 30, 2013 and consisted primarily of the repurchase of our common stock offset by the proceeds from the issuance of common stock in connection with the exercise of stock options by employees. Net cash provided by financing activities was \$11.2 million for the nine months ended September 30, 2012 and consisted primarily of the proceeds from the issuance of common stock in connection with the exercise of stock options by employees and the excess tax benefit from the exercise of employee stock options.

We have incurred significant expenses to develop our technology and services, to hire employees in our customer service, sales, marketing and administration departments, and for the amortization of purchased intangible assets, as well as non-cash compensation costs. Historically, we incurred significant quarterly net losses from inception through June 30, 2003, significant negative cash flows from operations in our quarterly periods from inception through December 31, 2002 and negative cash flows from operations of \$0.1 million in the three month period ended March 31, 2004. We also incurred a net loss and negative cash flow from operations in the quarterly period ended March 31, 2013 and a net loss in the quarterly periods ended June 30 and September 30, 2013. As of September 30, 2013, we had an accumulated deficit of approximately \$84.6 million. These losses have been funded primarily through the issuance of common stock in our initial public offering in 2000 and, prior to the initial public offering, the issuance of convertible preferred stock.

We anticipate that our current cash and cash equivalents will be sufficient to satisfy our working capital and capital requirements for at least the next 12 months. However, we cannot assure you that we will not require additional funds prior to such time, and we would then seek to sell additional equity or debt securities through public financings, or seek alternative sources of financing. We cannot assure you that additional funding will be available on favorable terms, when needed, if at all. If we are unable to obtain any necessary additional financing, we may be required to further reduce the scope of our planned sales and marketing and product development efforts, which could materially adversely affect our business, financial condition and operating results. In addition, we may require additional funds in

order to fund more rapid expansion, to develop new or enhanced services or products or to invest in or acquire complementary businesses, technologies, services or products.

Contractual Obligations and Commitments

We do not have any special purposes entities, and other than operating leases, which are described below, we do not engage in off-balance sheet financing arrangements.

We lease facilities and certain equipment under agreements accounted for as operating leases. These leases generally require us to pay all executory costs such as maintenance and insurance. Rental expense for operating leases for the three and

nine months ended September 30, 2013 was approximately \$2.2 million and \$6.9 million, respectively, and approximately \$2.0 million and \$5.3 million for the three and nine months ended September 30, 2012, respectively. As of September 30, 2013, our principal commitments were approximately \$23.8 million under various operating leases, of which approximately \$2.1 million is due in 2013. We currently expect that our principal commitments for the year ending December 31, 2013 will not exceed \$9.0 million in the aggregate.

Our contractual obligations at September 30, 2013 are summarized as follows:

Contractual Obligations	Payments due by period (in thousands)				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Operating leases	\$23,833	\$5,984	\$14,058	\$2,738	\$1,053
Total	\$23,833	\$5,984	\$14,058	\$2,738	\$1,053

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Currency Rate Fluctuations

As a result of the expanded scope of our Israeli operations, our currency rate fluctuation risk associated with the exchange rate movement of the U.S. dollar against the New Israeli Shekel (“NIS”) has increased. During the three months ended September 30, 2013, the U.S. dollar remained flat as compared to the NIS. During the nine months ended September 30, 2013, the U.S. dollar appreciated approximately 3%, as compared to the NIS. During the nine months ended September 30, 2013, expenses generated by our Israeli operations totaled approximately \$38.6 million. In addition, as we continue to increase our investment in the United Kingdom, Latin America, Western Europe and Asia-Pacific region, our currency rate fluctuation risk associated with the exchange rate movement of the U.S. dollar against the U.K. pound, Euro and AUS dollar has increased. We do not currently hedge our foreign currency risk exposure. We actively monitor the movement of the U.S. dollar against the NIS, U.K. pound, Euro, AUS dollar and Japanese Yen and have considered the use of financial instruments, including but not limited to derivative financial instruments, which could mitigate such risk. If we determine that our risk of exposure materially exceeds the potential cost of derivative financial instruments, we may in the future enter in to these types of investments. The functional currency of our wholly-owned Israeli subsidiaries, LivePerson Ltd. (formerly HumanClick Ltd.) and Kasamba Ltd., is the U.S. dollar; the functional currency of our operations in the United Kingdom is the U.K. pound; the functional currency of our operations in the Netherlands is the Euro; and the functional currency of our operations in Australia is the Australian Dollar.

Collection Risk

Our accounts receivable are subject, in the normal course of business, to collection risks. We regularly assess these risks and have established policies and business practices to protect against the adverse effects of collection risks. During the nine months ended September 30, 2013, we did not increase our allowance for doubtful accounts. During 2012, we increased our allowance for doubtful accounts by \$20,000 to approximately \$0.7 million, principally due to an increase in accounts receivable as a result of increased sales and, to a lesser extent, to an increase in the proportion of receivables due from customers with greater credit risk. A larger proportion of 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. We adjust our allowance for doubtful accounts when accounts previously reserved have been collected.

Interest Rate Risk

Our investments consist of cash and cash equivalents. Therefore, changes in the market’s interest rates do not affect in any material respect the value of the investments as recorded by us.

Inflation Risk

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

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, including the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our “disclosure controls and procedures,” as that term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), as of September 30, 2013. Based on that evaluation, the Chief Executive

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Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of September 30, 2013 to ensure that the information we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms, and to ensure that such information is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended September 30, 2013 identified in connection with the evaluation thereof by our management, including the Chief Executive Officer and Chief Financial Officer, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitations of the Effectiveness of Internal Control

A control system, no matter how well conceived and operated, can only provide reasonable, not absolute, assurance that the objectives of the internal control system are met. Because of the inherent limitations of any internal control system, no evaluation of controls can provide absolute assurance that all control issues, if any, have been detected.

Part II. Other Information

Item 1. Legal Proceedings

On February 7, 2012, we filed suit against Pragmatum Telecom LLC in the District of Delaware, seeking a declaratory judgment that our products do not infringe three patents owned by Pragmatum which Pragmatum had previously asserted were infringed by certain of our customers. On March 13, 2012, we amended the complaint to add a request for a declaratory judgment that those three patents are invalid. On April 6, 2012, Pragmatum answered the Amended Complaint, and asserted counterclaims against us asserting infringement of the same three patents and seeking unspecified monetary damages and injunctive relief. The Court entered a Scheduling Order on June 1, 2012 scheduling trial in this matter to begin on or after September 8, 2014. The matter is presently stayed until December 2013. We currently do not expect that the outcome of this matter will have a material adverse effect on our financial condition, results of operations or cash flows. However, litigation is inherently unpredictable; therefore, judgments could be rendered or settlements entered, that could adversely affect our operating results or cash flows in a particular period. Though it is reasonably possible that we will incur a liability associated with this litigation, the amount of any such liability is not reasonably estimable at this time.

We routinely assess all of our litigation and threatened litigation as to the probability of ultimately incurring a liability, and record our best estimate of the ultimate loss in situations where we assess the likelihood of loss as probable.

From time to time, we are 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 us with respect to intellectual property, contracts, employment and other matters, as well as claims brought against our customers for whom we have a contractual indemnification obligation. We accrue 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 we determine that a loss is not probable, but is reasonably possible, and it becomes possible to develop what we believe to be a reasonable range of possible loss, then we will include disclosures 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, we 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 our financial statements as a whole or, if the amount of such adjustment cannot be reasonably estimated, disclose that an estimate cannot be made.

Item 1A. Risk Factors

Risks that could have a material and adverse impact on our business, results of operations and financial condition include the following: potential fluctuations in our quarterly revenue and operating results; the adverse effect that the

global economic downturn may have on our business and results of operations; competition in the markets for online sales, marketing and customer service solutions, and online consumer services; our ability to retain existing customers and attract new customers; risks related to new regulatory or other legal requirements that could materially impact our business; impairments to goodwill that result in significant charges to earnings; volatility of the value of certain currencies in relation to the U.S. dollar, particularly the New Israeli Shekel, U.K. pound, Euro, Australian Dollar and Japanese Yen; additional regulatory requirements, tax liabilities, currency exchange rate fluctuations and other risks as we expand internationally; responding to rapid technological change and changing customer preferences; our ability to retain key personnel and attract new personnel; our ability to expand our operations internationally; risks related to the ability to successfully integrate past or potential future acquisitions; risks related to failures or

security breaches in our services, those of our third party providers, or in the websites of our customers; risks related to the regulation or possible misappropriation of personal information belonging to our customers' Internet users; technology systems beyond our control and technology-related defects that could disrupt the LivePerson services; privacy concerns relating to the Internet that could result in new legislation or negative public perception; legal liability and/or negative publicity for the services provided to consumers via our technology platforms; risks related to protecting our intellectual property rights or potential infringement of the intellectual property rights of third parties; increased allowances for doubtful accounts as a result of an increasing amount of receivables due from customers with greater credit risk; delays in our implementation cycles; risks associated with our current or future stock repurchase programs, including whether such programs will enhance long-term stockholder value, and whether such stock repurchases could increase the volatility of the price of our common stock and diminish our cash reserves; risks related to our international operations, particularly our operations in Israel, and the civil and political unrest in that region; and risks related to our common stock being traded on more than one securities exchange, which may result in additional variations in the trading price of our common stock. This list is intended to identify only certain of the principal factors that could have a material and adverse impact on our business, results of operations and financial condition. A more detailed description of each of these and other important risk factors can be found under the caption "Risk Factors" in our most recent Annual Report on Form 10-K filed on March 1, 2013 (the "Form 10-K").

There are no material changes to the risk factors described in the Form 10-K.

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

Unregistered Sales of Equity Securities

None.

Purchase of Equity Securities by the Issuer

The following table presents information regarding our purchases of our common stock for the three months ended September 30, 2013:

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share (1)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (1) (2)
7/1/2013 – 7/31/2013	—	—	—	\$3,474,027
8/1/2013 – 8/31/2013	18,900	\$9.98	18,900	3,284,387
9/1/2013 – 9/30/2013	—	—	—	3,284,387
Total	18,900	\$9.98	18,900	\$3,284,387

On December 10, 2012, the Company announced that its Board of Directors approved a share repurchase program through June 30, 2014. On May 21, 2013, our Board of Directors extended the aggregate purchase price of the stock repurchase program. Under the stock repurchase program, the Company is authorized to repurchase shares of (1) the Company's 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, up to an aggregate purchase price of \$30.0 million. As of September 30, 2013, approximately \$3.3 million remained available for purchases under the program.

(2) Transaction fees related to the share purchases are deducted from the total remaining allowable expenditure amount.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

ITEM 6. EXHIBITS

The following exhibits are filed as part of this Quarterly Report on Form 10-Q:

- | | |
|----------|--|
| 31.1 | Certification by Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification by Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.1** | Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2** | Certification by Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 101.INS† | XBRL Instance Document |
| 101.SCH† | XBRL Taxonomy Extension Schema Document |
| 101.CAL† | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF† | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB† | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE† | XBRL Taxonomy Extension Presentation Linkbase Document |

** These certifications are not deemed filed with the Securities and Exchange Commission and are not to be incorporated by reference in any filing we make under the Securities Act of 1933 or the Securities Exchange Act of 1934, irrespective of any general incorporation language in any filings.

† In accordance with Rule 406T of Regulation S-T, these XBRL (eXtensible Business Reporting Language) documents are furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability under these sections.

SIGNATURES

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

LIVEPERSON, INC.
(Registrant)

Date: November 7, 2013

By: /s/ ROBERT P. LOCASCIO
Name: Robert P. LoCascio
Title: Chief Executive Officer (principal executive officer)

Date: November 7, 2013

By: /s/ DANIEL R. MURPHY
Name: Daniel R. Murphy
Title: Chief Financial Officer (principal financial and accounting officer)

EXHIBIT INDEX
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