

ELLIE MAE INC  
Form 10-Q  
August 03, 2017  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

OR

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

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

Commission File Number: 001-35140

ELLIE MAE, INC.

(Exact name of registrant as specified in its charter)

Delaware 94-3288780  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

4420 Rosewood Drive, Suite 500 94588  
Pleasanton, California (Zip Code)  
(Address of principal executive offices) (925) 227-7000  
(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 (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

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

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If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. Yes  No

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

Indicate the number of shares outstanding of each of the registrant's classes of common stock as of the latest practicable date:

As of August 1, 2017:

| Class                            | Number of Shares |
|----------------------------------|------------------|
| Common Stock, \$0.0001 par value | 34,378,495       |

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## PART I—FINANCIAL INFORMATION

## ITEM 1—CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Ellie Mae, Inc.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(in thousands, except share and per share amounts)

|                                                                                                                                                                                            | June 30,<br>2017 | December 31,<br>2016 |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------|----------------------|
| Assets                                                                                                                                                                                     |                  |                      |
| Current assets:                                                                                                                                                                            |                  |                      |
| Cash and cash equivalents                                                                                                                                                                  | \$213,204        | \$ 380,907           |
| Short-term investments                                                                                                                                                                     | 120,454          | 41,841               |
| Accounts receivable, net of allowance for doubtful accounts of \$249 and \$45 as of June 30, 2017 and December 31, 2016, respectively                                                      | 45,542           | 39,358               |
| Prepaid expenses and other current assets                                                                                                                                                  | 18,965           | 15,209               |
| Total current assets                                                                                                                                                                       | 398,165          | 477,315              |
| Property and equipment, net                                                                                                                                                                | 156,698          | 126,297              |
| Long-term investments                                                                                                                                                                      | 121,096          | 45,931               |
| Intangible assets, net                                                                                                                                                                     | 15,133           | 17,289               |
| Deposits and other assets                                                                                                                                                                  | 22,705           | 10,138               |
| Goodwill                                                                                                                                                                                   | 74,547           | 74,547               |
| Total assets                                                                                                                                                                               | \$788,344        | \$ 751,517           |
| Liabilities and Stockholders' Equity                                                                                                                                                       |                  |                      |
| Current liabilities:                                                                                                                                                                       |                  |                      |
| Accounts payable                                                                                                                                                                           | \$15,831         | \$ 15,942            |
| Accrued and other current liabilities                                                                                                                                                      | 22,901           | 39,809               |
| Deferred revenue                                                                                                                                                                           | 17,985           | 23,126               |
| Total current liabilities                                                                                                                                                                  | 56,717           | 78,877               |
| Leases payable, net of current portion                                                                                                                                                     | 28               | 85                   |
| Other long-term liabilities                                                                                                                                                                | 16,424           | 17,647               |
| Total liabilities                                                                                                                                                                          | 73,169           | 96,609               |
| Commitments and contingencies (Note 8)                                                                                                                                                     |                  |                      |
| Stockholders' equity:                                                                                                                                                                      |                  |                      |
| Common stock, \$0.0001 par value per share; 140,000,000 authorized shares, 34,320,850 and 33,685,649 shares issued and outstanding as of June 30, 2017 and December 31, 2016, respectively | 3                | 3                    |
| Additional paid-in capital                                                                                                                                                                 | 629,443          | 612,098              |
| Accumulated other comprehensive loss                                                                                                                                                       | (264             | ) (219               |
| Retained earnings                                                                                                                                                                          | 85,993           | 43,026               |
| Total stockholders' equity                                                                                                                                                                 | 715,175          | 654,908              |
| Total liabilities and stockholders' equity                                                                                                                                                 | \$788,344        | \$ 751,517           |

See accompanying notes to these condensed consolidated financial statements (unaudited).

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Ellie Mae, Inc.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

(in thousands, except share and per share amounts)

|                                                                                        | Three Months ended |            | Six Months ended |            |
|----------------------------------------------------------------------------------------|--------------------|------------|------------------|------------|
|                                                                                        | June 30,           |            | June 30,         |            |
|                                                                                        | 2017               | 2016       | 2017             | 2016       |
| Revenues                                                                               | \$ 104,125         | \$ 90,098  | \$ 197,127       | \$ 163,723 |
| Cost of revenues                                                                       | 38,267             | 28,453     | 73,035           | 55,084     |
| Gross profit                                                                           | 65,858             | 61,645     | 124,092          | 108,639    |
| Operating expenses:                                                                    |                    |            |                  |            |
| Sales and marketing                                                                    | 13,860             | 12,506     | 33,240           | 27,792     |
| Research and development                                                               | 16,046             | 14,662     | 33,453           | 27,115     |
| General and administrative                                                             | 18,727             | 17,793     | 35,669           | 33,525     |
| Total operating expenses                                                               | 48,633             | 44,961     | 102,362          | 88,432     |
| Income from operations                                                                 | 17,225             | 16,684     | 21,730           | 20,207     |
| Other income, net                                                                      | 762                | 162        | 1,263            | 361        |
| Income before income taxes                                                             | 17,987             | 16,846     | 22,993           | 20,568     |
| Income tax provision (benefit)                                                         | (836 )             | 6,258      | (5,429 )         | 7,474      |
| Net income                                                                             | \$ 18,823          | \$ 10,588  | \$ 28,422        | \$ 13,094  |
| Net income per share of common stock:                                                  |                    |            |                  |            |
| Basic                                                                                  | \$ 0.55            | \$ 0.36    | \$ 0.84          | \$ 0.44    |
| Diluted                                                                                | \$ 0.52            | \$ 0.34    | \$ 0.79          | \$ 0.42    |
| Weighted average common shares used in computing net income per share of common stock: |                    |            |                  |            |
| Basic                                                                                  | 34,028,553         | 29,578,630 | 33,866,233       | 29,643,779 |
| Diluted                                                                                | 35,908,813         | 31,188,599 | 35,771,565       | 31,279,512 |
| Net income                                                                             | \$ 18,823          | \$ 10,588  | \$ 28,422        | \$ 13,094  |
| Other comprehensive income, net of taxes:                                              |                    |            |                  |            |
| Unrealized gain (loss) on investments                                                  | (103 )             | 101        | (45 )            | 429        |
| Comprehensive income                                                                   | \$ 18,720          | \$ 10,689  | \$ 28,377        | \$ 13,523  |

See accompanying notes to these condensed consolidated financial statements (unaudited).

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Ellie Mae, Inc.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(in thousands)

|                                                                                   | Six Months ended<br>June 30, |                 |
|-----------------------------------------------------------------------------------|------------------------------|-----------------|
|                                                                                   | 2017                         | 2016            |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                      |                              |                 |
| Net income                                                                        | \$28,422                     | \$13,094        |
| Adjustments to reconcile net income to net cash provided by operating activities: |                              |                 |
| Depreciation and amortization                                                     | 16,282                       | 8,679           |
| Amortization of intangible assets                                                 | 2,156                        | 2,949           |
| Stock-based compensation expense                                                  | 16,361                       | 14,708          |
| Deferred income taxes                                                             | (5,662)                      | ) 6,153         |
| Loss on disposal of property and equipment                                        | —                            | 5               |
| Amortization (accretion) of investments                                           | (139)                        | ) 490           |
| Changes in operating assets and liabilities:                                      |                              |                 |
| Accounts receivable, net                                                          | (6,183)                      | ) (15,738)      |
| Prepaid expenses and other current assets                                         | (3,757)                      | ) (1,388)       |
| Deposits and other assets                                                         | 194                          | (1,580)         |
| Accounts payable                                                                  | 2,677                        | (432)           |
| Accrued, other current and other liabilities                                      | (10,243)                     | ) (6,629)       |
| Deferred revenue                                                                  | (5,087)                      | ) 2,895         |
| Net cash provided by operating activities                                         | 35,021                       | 23,206          |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                      |                              |                 |
| Acquisition of property and equipment                                             | (21,800)                     | ) (15,566)      |
| Acquisition of internal-use software                                              | (25,478)                     | ) (16,373)      |
| Purchases of investments                                                          | (181,760)                    | ) (35,615)      |
| Maturities of investments                                                         | 28,076                       | 31,551          |
| Sale of investments                                                               | —                            | 20,000          |
| Net cash used in investing activities                                             | (200,962)                    | ) (16,003)      |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                      |                              |                 |
| Payment of capital lease obligations                                              | (553)                        | ) (2,080)       |
| Proceeds from issuance of common stock under employee stock plans                 | 10,207                       | 9,127           |
| Payment of issuance costs relating to common stock issued in public offering      | (15)                         | )—              |
| Tax payments related to shares withheld for vested restricted stock units         | (11,401)                     | ) (4,037)       |
| Net cash provided by (used in) financing activities                               | (1,762)                      | ) 3,010         |
| <b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>                       | <b>(167,703)</b>             | <b>) 10,213</b> |
| <b>CASH AND CASH EQUIVALENTS, Beginning of period</b>                             | <b>380,907</b>               | <b>34,396</b>   |
| <b>CASH AND CASH EQUIVALENTS, End of period</b>                                   | <b>\$213,204</b>             | <b>\$44,609</b> |
| <b>Supplemental disclosure of cash flow information:</b>                          |                              |                 |
| Cash paid for interest                                                            | \$370                        | \$145           |
| Cash paid for income taxes                                                        | \$463                        | \$129           |
| <b>Supplemental disclosure of non-cash investing and financing activities:</b>    |                              |                 |
| Fixed asset purchases accrued but not paid                                        | \$3,172                      | \$3,709         |
| Stock-based compensation capitalized to property and equipment                    | \$2,178                      | \$1,125         |

See accompanying notes to these condensed consolidated financial statements (unaudited).



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Ellie Mae, Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

NOTE 1—Description of Business

Ellie Mae, Inc. (“Ellie Mae,” the “Company,” “we,” “our” or “us”) is a leading provider of innovative on-demand software solutions and services for the residential mortgage industry in the United States. Banks, credit unions and mortgage lenders use the Company’s Encompass® all-in-one mortgage management solution (“Encompass”) to originate and fund mortgages and improve compliance, loan quality, and efficiency.

NOTE 2—Basis of Presentation and Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (“U.S. GAAP”) and applicable rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain information and note disclosures included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016, which was filed with the SEC on February 22, 2017 (“2016 Form 10-K”). The condensed consolidated balance sheet as of December 31, 2016, included herein, was derived from the audited financial statements as of that date but does not include all disclosures, including notes, required by U.S. GAAP. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial position, results of operations and cash flows for the interim periods but are not necessarily indicative of the results of operations to be anticipated for the full fiscal year ending December 31, 2017, or any future period.

Principles of Consolidation

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

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Management evaluates estimates on a regular basis including those relating to revenue recognition, allowance for doubtful accounts, goodwill, intangible assets, valuation of deferred income taxes, stock-based compensation, and unrecognized tax benefits, among others. Actual results could differ from those estimates, and such differences may have a material impact on the Company’s condensed consolidated financial statements and footnotes.

Significant Accounting Policies

The Company’s significant accounting policies are described in Note 2 of the Notes to Consolidated Financial Statements in its 2016 Form 10-K. There have been no significant changes to these policies during the six months ended June 30, 2017, except in relation to the Company’s adoption of ASU No. 2016-09, Compensation—Stock Compensation (Topic 718): Improvements to Employee Shared-Based Payment Accounting (“ASU 2016-09”) on January 1, 2017, whereby the Company now records excess tax benefits and tax deficiencies as an income tax benefit or expense when stock awards vest or settle, and the Company no longer classifies the cash flow from excess tax benefits as a reduction from operating cash flows. This resulted in a \$1.2 million increase in net cash provided by operating activities and a corresponding \$1.2 million decrease in net cash provided by financing activities for the six months ended June 30, 2016.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes certain changes in equity that are excluded from net income, specifically unrealized gains on marketable securities. Except for net realized gain on investments, which was not significant, there were no reclassifications out of accumulated other comprehensive income that affected net income during the three and six months ended June 30,



2017 and 2016.

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### Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers (“ASU 2014-09”), which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. This standard also requires significantly expanded disclosures about revenue recognition. The effective date for public entities is fiscal years beginning after December 15, 2017 and early adoption is allowed. The Company will adopt the new standard as of January 1, 2018. The guidance permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (modified retrospective method).

The Company is continuing to evaluate the impact of the new standard on its accounting policies, processes, and systems, including impacts from guidance issued by the FASB Transition Resource Group as part of its November 2016 meeting. The Company has assigned internal resources, engaged a third-party service provider, and is in the process of finalizing the evaluation and completing the implementation.

The Company expects an impact to certain revenue streams due to the removal of the current limitation on contingent revenue, which may affect the timing of revenues being recognized for certain contracts. The Company has also identified potential impacts to the costs to obtain contracts, which is primarily comprised of sales commissions and the related fringe benefits associated with non-cancelable contracts. The Company expects to capitalize certain costs that are expensed under the current standard, and the Company expects an increase in the amortization period over which the capitalized costs will be recognized. The Company is continuing to evaluate the impact to the expected period of benefit under ASU 2014-09.

The Company is evaluating the adoption method based on various factors including the significance of the impact of the new standard on the Company’s financial results and system capabilities. This evaluation is in process, and the adoption method has not been determined.

In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities (“ASU 2016-01”), which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, and early adoption is not permitted. The Company is currently evaluating the impact of this accounting standard update on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (“ASU 2016-02”), which requires lessees to put most leases on their balance sheets but recognize the expenses on their income statements in a manner similar to current practice. ASU 2016-02 states that a lessee would recognize a lease liability for the obligation to make lease payments and a right-to-use asset for the right to use the underlying asset for the lease term. The standard is effective for interim and annual periods beginning after December 15, 2018, and early adoption is permitted. The Company currently does not intend to early adopt and is evaluating the impact of this accounting standard update on its consolidated financial statements.

In May 2017, the FASB issued ASU No. 2017-09, Compensation – Stock Compensation (Topic 718): Scope of Modification Accounting (“ASU 2017-09”), which provides guidance on determining which changes to the terms and conditions of share-based payment awards require an entity to apply modification accounting under Topic 718. ASU 2017-09 is effective for interim and annual periods beginning after December 15, 2017, and early adoption is permitted. The Company is currently evaluating the impact of this accounting standard update on its consolidated financial statements.

### New Standards Adopted

In January 2017, the FASB issued ASU No. 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business. This standard clarifies the definition of a business and is intended to help companies evaluate whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The standard is effective for interim and annual periods beginning after December 15, 2017 and early adoption is permitted under certain circumstances. The standard should be applied prospectively as of the beginning of the period of adoption. The

Company has elected to early adopt the standard on April 1, 2017. The adoption did not have an impact on the Company's consolidated financial statements as there have been no business combinations in fiscal year 2017 to date.

**NOTE 3—Net Income Per Share of Common Stock**

Net income per share of common stock is calculated by dividing net income by the weighted average shares of common stock outstanding during the period. Diluted net income per share of common stock is calculated by dividing net income by the weighted average shares of common stock outstanding and potential shares of common stock during the period. Potential shares of common stock include dilutive shares attributable to the assumed exercise of stock options, restricted stock unit awards ("RSUs"), performance-vesting RSUs, performance share awards ("Performance Awards"), and Employee Stock Purchase Plan ("ESPP") shares using the treasury stock method, if dilutive.

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The components of net income per share of common stock were as follows:

|                                                                                            | Three Months<br>ended June 30,                     |            | Six Months ended<br>June 30, |            |
|--------------------------------------------------------------------------------------------|----------------------------------------------------|------------|------------------------------|------------|
|                                                                                            | 2017                                               | 2016       | 2017                         | 2016       |
|                                                                                            | (in thousands, except share and per share amounts) |            |                              |            |
| Net income                                                                                 | \$18,823                                           | \$ 10,588  | \$28,422                     | \$ 13,094  |
| Basic shares:                                                                              |                                                    |            |                              |            |
| Weighted average common shares outstanding                                                 | 34,028,552                                         | 29,578,630 | 33,866,232                   | 29,643,779 |
| Diluted shares:                                                                            |                                                    |            |                              |            |
| Weighted average shares used to compute basic net income per share                         | 34,028,552                                         | 29,578,630 | 33,866,232                   | 29,643,779 |
| Effect of potentially dilutive securities:                                                 |                                                    |            |                              |            |
| Employee stock options, RSUs, performance-vesting RSUs, Performance Awards and ESPP shares | 1,880,260                                          | 1,609,969  | 1,905,332                    | 1,635,733  |
| Weighted average shares used to compute diluted net income per share                       | 35,908,812                                         | 31,188,599 | 35,771,564                   | 31,279,512 |
| Net income per share:                                                                      |                                                    |            |                              |            |
| Basic                                                                                      | \$0.55                                             | \$ 0.36    | \$0.84                       | \$ 0.44    |
| Diluted                                                                                    | \$0.52                                             | \$ 0.34    | \$0.79                       | \$ 0.42    |

The following potential weighted average common shares were excluded from the computation of diluted net income per share, as their effect would have been anti-dilutive:

|                                   | Three<br>Months<br>ended June<br>30, |        | Six Months<br>ended June 30, |         |
|-----------------------------------|--------------------------------------|--------|------------------------------|---------|
|                                   | 2017                                 | 2016   | 2017                         | 2016    |
| Employee stock options and awards | 6,601                                | 31,721 | 110,587                      | 237,177 |

Performance-vesting RSUs and Performance Awards are included in the diluted shares outstanding for each period if the established performance criteria have been met at the end of the respective periods. However, if none of the required performance criteria have been met for such awards, the Company includes the number of shares that would be issuable if the end of the reporting period were the end of the contingency period. Accordingly, in addition to the employee stock options and awards noted above, 61,494 and 136,598 shares underlying performance-vesting RSUs and Performance Awards were excluded from the dilutive shares outstanding for each of the three and six months ended June 30, 2017 and 2016, respectively.

**NOTE 4—Financial Instruments and Fair Value Measurements**

Fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are classified and disclosed in one of the following three categories:

Level 1 — Valuations based on quoted prices in active markets for identical assets or liabilities.

Level 2 — Valuations based on other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 — Valuations based on inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the assets or liabilities.

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The following tables set forth by level within the fair value hierarchy the Company's financial assets that were accounted for at fair value on a recurring basis:

|                                                   | June 30, 2017             |           |           | December 31, 2016         |           |           |
|---------------------------------------------------|---------------------------|-----------|-----------|---------------------------|-----------|-----------|
|                                                   | Level 1<br>(in thousands) | Level 2   | Total     | Level 1<br>(in thousands) | Level 2   | Total     |
| Cash equivalents:                                 |                           |           |           |                           |           |           |
| Money market funds                                | \$122,123                 | \$—       | \$122,123 | \$2,733                   | \$—       | \$2,733   |
| Corporate notes and obligations                   | —                         | 18,367    | 18,367    | —                         | —         | —         |
| U.S. government and government agency obligations | 9,898                     | 7,094     | 16,992    | 151,660                   | 149,976   | 301,636   |
| Investments:                                      |                           |           |           |                           |           |           |
| Certificates of deposit                           | —                         | 9,975     | 9,975     | —                         | 12,088    | 12,088    |
| Corporate notes and obligations                   | —                         | 73,647    | 73,647    | —                         | 28,892    | 28,892    |
| Municipal obligations                             | —                         | 10,915    | 10,915    | —                         | 11,361    | 11,361    |
| U.S. government and government agency obligations | 46,497                    | 100,516   | 147,013   | 4,579                     | 30,852    | 35,431    |
|                                                   | \$178,518                 | \$220,514 | \$399,032 | \$158,972                 | \$233,169 | \$392,141 |

The Company classifies its money market funds that are specifically backed by debt securities and U.S. government obligations as Level 1 instruments, due to the use of observable market prices for identical securities that are traded in active markets.

Valuation of the Company's marketable securities investments classified as Level 2 is achieved primarily through broker quotes when such investments exist in a non-active market.

At June 30, 2017 and December 31, 2016, the Company did not have any assets or liabilities that were valued using Level 3 inputs. For the three and six months ended June 30, 2017 and 2016, there were no transfers of financial instruments between the levels.

Realized gains and losses from the sale of investments were not significant during the three and six months ended June 30, 2017 and 2016.

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The carrying amounts, gross unrealized gains and losses and estimated fair value of cash and cash equivalents and both short-term and long-term investments consisted of the following:

|                                                   | June 30, 2017                    |                  |                   | December 31, 2016      |                                  |                  |                   |                        |
|---------------------------------------------------|----------------------------------|------------------|-------------------|------------------------|----------------------------------|------------------|-------------------|------------------------|
|                                                   | Amortized Cost<br>(in thousands) | Unrealized Gains | Unrealized Losses | Carrying or Fair Value | Amortized Cost<br>(in thousands) | Unrealized Gains | Unrealized Losses | Carrying or Fair Value |
| <b>Cash and cash equivalents:</b>                 |                                  |                  |                   |                        |                                  |                  |                   |                        |
| Cash                                              | \$55,722                         | \$ —             | \$ —              | \$55,722               | \$76,538                         | \$ —             | \$ —              | \$76,538               |
| Money market funds                                | 122,123                          | —                | —                 | 122,123                | 2,733                            | —                | —                 | 2,733                  |
| Corporate notes and obligations                   | 18,367                           | —                | —                 | 18,367                 | —                                | —                | —                 | —                      |
| U.S. government and government agency obligations | 16,992                           | —                | —                 | 16,992                 | 301,631                          | 8                | (3 )              | 301,636                |
|                                                   | \$213,204                        | \$ —             | \$ —              | \$213,204              | \$380,902                        | \$ 8             | \$ (3 )           | \$380,907              |
| <b>Investments:</b>                               |                                  |                  |                   |                        |                                  |                  |                   |                        |
| Corporate notes and obligations                   | \$73,756                         | \$ 5             | \$ (114 )         | \$73,647               | \$28,978                         | \$ 1             | \$ (87 )          | \$28,892               |
| Certificates of deposit                           | 9,973                            | 3                | (1 )              | 9,975                  | 12,094                           | 13               | (19 )             | 12,088                 |
| Municipal obligations                             | 10,919                           | 10               | (14 )             | 10,915                 | 11,422                           | 1                | (62 )             | 11,361                 |
| U.S. government and government agency obligations | 147,166                          | 3                | (156 )            | 147,013                | 35,502                           | 8                | (79 )             | 35,431                 |
|                                                   | \$241,814                        | \$ 21            | \$ (285 )         | \$241,550              | \$87,996                         | \$ 23            | \$ (247 )         | \$87,772               |

The following table shows the gross unrealized losses and the related fair values of the Company's investments that have been in a continuous unrealized loss position. The Company did not identify any investments as other-than-temporarily impaired at June 30, 2017 or December 31, 2016.

|                                                               | June 30, 2017       |                   |                      |                   |            |                   |
|---------------------------------------------------------------|---------------------|-------------------|----------------------|-------------------|------------|-------------------|
|                                                               | Less than 12 Months |                   | 12 Months or Greater |                   | Total      |                   |
|                                                               | Fair Value          | Unrealized Losses | Fair Value           | Unrealized Losses | Fair Value | Unrealized Losses |
|                                                               | (in thousands)      |                   |                      |                   |            |                   |
| Corporate notes and obligations                               | \$63,252            | \$ (108 )         | \$659                | \$ (6 )           | \$63,911   | \$ (114 )         |
| Certificates of deposit                                       | 3,150               | —                 | 485                  | (1 )              | 3,635      | (1 )              |
| U.S. government, government agency, and municipal obligations | 146,580             | (165 )            | 839                  | (5 )              | 147,419    | (170 )            |
|                                                               | \$212,982           | \$ (273 )         | \$1,983              | \$ (12 )          | \$214,965  | \$ (285 )         |
|                                                               | December 31, 2016   |                   |                      |                   |            |                   |
|                                                               | Less than 12 Months |                   | 12 Months or Greater |                   | Total      |                   |
|                                                               | Fair Value          | Unrealized Losses | Fair Value           | Unrealized Losses | Fair Value | Unrealized Losses |
|                                                               | (in thousands)      |                   |                      |                   |            |                   |
| Corporate notes and obligations                               | \$26,076            | \$ (87 )          | \$—                  | \$ —              | \$26,076   | \$ (87 )          |
| Certificates of deposit                                       | 5,651               | (19 )             | —                    | —                 | 5,651      | (19 )             |
| U.S. government, government agency, and municipal obligations | 180,138             | (144 )            | 385                  | —                 | 180,523    | (144 )            |
|                                                               | \$211,865           | \$ (250 )         | \$385                | \$ —              | \$212,250  | \$ (250 )         |

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The following table summarizes the maturities of the Company's investments at June 30, 2017:

|                   | Carrying or<br>Fair Value<br>(in<br>thousands) |
|-------------------|------------------------------------------------|
| Remainder of 2017 | \$ 66,031                                      |
| 2018              | 87,471                                         |
| 2019              | 64,577                                         |
| 2020              | 23,471                                         |
| Total             | \$ 241,550                                     |

Actual maturities may differ from the contractual maturities because borrowers may have the right to call or prepay certain obligations.

## NOTE 5—Balance Sheet Components

## Property and Equipment

Property and equipment, net, consisted of the following:

|                                                              | June 30,<br>2017<br>(in thousands) | December<br>31,<br>2016 |
|--------------------------------------------------------------|------------------------------------|-------------------------|
| Computer equipment and software <sup>(1)</sup>               | \$ 156,390                         | \$ 116,602              |
| Furniture and fixtures                                       | 8,960                              | 6,838                   |
| Leasehold improvements                                       | 28,229                             | 18,532                  |
| Property and equipment                                       | 193,579                            | 141,972                 |
| Accumulated depreciation and amortization <sup>(1)</sup>     | (65,273 )                          | (48,991 )               |
| Subtotal                                                     | 128,306                            | 92,981                  |
| Internal-use software and other assets not placed in service | 28,392                             | 33,316                  |
| Property and equipment, net                                  | \$ 156,698                         | \$ 126,297              |

<sup>(1)</sup> Includes computer equipment and software under capital leases

Computer equipment and software under capital leases, net, consisted of the following:

|                                                          | June 30,<br>2017<br>(in thousands) | December<br>31,<br>2016 |
|----------------------------------------------------------|------------------------------------|-------------------------|
| Computer equipment                                       | \$ 8,715                           | \$ 8,715                |
| Software                                                 | 1,517                              | 1,517                   |
| Accumulated depreciation and amortization                | (8,033 )                           | (6,522 )                |
| Net computer equipment and software under capital leases | \$ 2,199                           | \$ 3,710                |

Depreciation and amortization expense for the three and six months ended June 30, 2017 was \$8.9 million and \$16.3 million, respectively. Depreciation and amortization expense for the three and six months ended June 30, 2016 was \$4.7 million and \$8.7 million, respectively. Depreciation and amortization of assets under capital leases which is included in the depreciation and amortization expense for the three and six months ended June 30, 2017 was \$0.8 million and \$1.5 million, respectively. Depreciation and amortization of assets under capital leases which is included in depreciation and amortization expense for the three and six months ended June 30, 2016 was \$0.8 million and \$1.6 million, respectively.

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## Accrued and Other Current Liabilities

Accrued and other current liabilities consisted of the following:

|                                          | June 30,<br>2017 | December<br>31,<br>2016 |
|------------------------------------------|------------------|-------------------------|
|                                          | (in thousands)   |                         |
| Accrued payroll and related expenses     | \$ 16,400        | \$ 31,848               |
| Accrued commissions                      | 1,036            | 1,832                   |
| Accrued royalties                        | 2,264            | 1,395                   |
| Sales and other taxes                    | 1,328            | 2,327                   |
| Other accrued liabilities <sup>(1)</sup> | 1,873            | 2,407                   |
|                                          | \$22,901         | \$ 39,809               |

<sup>(1)</sup> Certain reclassifications of prior period amounts have been made to conform to the current period presentation, such reclassification did not materially change previously reported consolidated financial statements.



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## NOTE 6— Goodwill and Intangible Assets

The carrying value of goodwill at June 30, 2017 was \$74.5 million. There were no changes in the carrying value of goodwill during the three and six months ended June 30, 2017.

Intangible assets, net, consisted of the following:

|                                       | June 30, 2017         |                          |                 |                                        |
|---------------------------------------|-----------------------|--------------------------|-----------------|----------------------------------------|
|                                       | Gross Carrying Amount | Accumulated Amortization | Net Intangibles | Weighted Average Remaining Useful Life |
|                                       | (in thousands)        |                          |                 | (in years)                             |
| Assets subject to amortization:       |                       |                          |                 |                                        |
| Developed technology                  | \$ 11,535             | \$ (8,849 )              | \$ 2,686        | 2.3                                    |
| Trade names                           | 331                   | (331 )                   | —               | 0.0                                    |
| Customer relationships                | 19,400                | (11,206 )                | 8,194           | 3.6                                    |
| Order backlog                         | 370                   | (156 )                   | 214             | 2.3                                    |
| Total assets subject to amortization: | 31,636                | (20,542 )                | 11,094          | 3.2                                    |
| Assets not subject to amortization:   |                       |                          |                 |                                        |
| Trade name                            | 4,039                 | —                        | 4,039           |                                        |
|                                       | \$35,675              | \$ (20,542 )             | \$ 15,133       |                                        |

|                                       | December 31, 2016     |                          |                 |                                        |
|---------------------------------------|-----------------------|--------------------------|-----------------|----------------------------------------|
|                                       | Gross Carrying Amount | Accumulated Amortization | Net Intangibles | Weighted Average Remaining Useful Life |
|                                       | (in thousands)        |                          |                 | (in years)                             |
| Assets subject to amortization:       |                       |                          |                 |                                        |
| Developed technology                  | \$ 11,535             | \$ (8,183 )              | \$ 3,352        | 2.7                                    |
| Trade names                           | 331                   | (331 )                   | —               | 0.0                                    |
| Customer relationships                | 19,400                | (9,762 )                 | 9,638           | 4.0                                    |
| Order backlog                         | 370                   | (110 )                   | 260             | 2.8                                    |
| Total assets subject to amortization: | 31,636                | (18,386 )                | 13,250          | 3.6                                    |
| Assets not subject to amortization:   |                       |                          |                 |                                        |
| Trade name                            | 4,039                 | —                        | 4,039           |                                        |
|                                       | \$35,675              | \$ (18,386 )             | \$ 17,289       |                                        |

Amortization expense associated with intangible assets for the three and six months ended June 30, 2017 was \$1.1 million and \$2.2 million, respectively. Amortization expense associated with intangible assets for the three and six months ended June 30, 2016 was \$1.5 million and \$2.9 million, respectively.

Future amortization expense for intangible assets at June 30, 2017 was as follows:

|                   | Amortization<br>(in thousands) |
|-------------------|--------------------------------|
| Remainder of 2017 | \$ 2,138                       |
| 2018              | 3,443                          |
| 2019              | 3,166                          |
| 2020              | 1,778                          |
| 2021              | 314                            |
| 2022              | 255                            |
|                   | \$ 11,094                      |

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## NOTE 7—Income Taxes

The Company computes its interim provision for income taxes by applying the estimated annual effective tax rate to the year-to-date income from recurring operations and adjusts the provision for discrete tax items recorded in the period. The Company evaluates and updates its estimated annual effective income tax rate on a quarterly basis. The estimated annual effective tax rate as of June 30, 2017 and 2016 was 35.8% and 37.4%, respectively.

|                                   | Three Months<br>ended June 30, |         | Six Months ended<br>June 30, |         |
|-----------------------------------|--------------------------------|---------|------------------------------|---------|
|                                   | 2017                           | 2016    | 2017                         | 2016    |
|                                   | (dollars in<br>thousands)      |         | (dollars in thousands)       |         |
| Income tax provision (benefit)    | \$(836)                        | \$6,258 | \$(5,429)                    | \$7,474 |
| Effective tax rate <sup>(1)</sup> | (4.7 )%                        | 37.2 %  | (23.6 )%                     | 36.3 %  |

<sup>(1)</sup> The impact to the effective tax rate due to the benefit of excess stock award deductions allowable under ASU 2016-09 is 40.9% and 60.1% for the three and six months ended June 30, 2017, respectively.

The difference between the federal statutory rate of 35% and the Company's estimated effective tax rate for the three and six months ended June 30, 2017 was primarily due to the benefit of excess stock award deductions in tax expense allowable under ASU 2016-09, R&D credits, and non-deductible stock-based compensation expenses.

As described in Note 2 "Basis of Presentation and Significant Accounting Policies", the Company adopted ASU 2016-09 on January 1, 2017, which requires the excess tax benefits or deficiencies to be reflected in the Consolidated Statements of Comprehensive Income as a component of the provision for income taxes, which were previously recognized in equity. Total excess tax benefits recognized for the three and six months ended June 30, 2017 was \$7.3 million and \$13.8 million, respectively.

The Company's tax positions are subject to income tax audits by multiple tax jurisdictions. The Company accounts for uncertain tax positions and believes that it has provided adequate reserves for its unrecognized tax benefits for all tax years still open for assessment. The Company also believes that it does not have any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease within the next twelve months.

The Company has a policy to classify accrued interest and penalties associated with uncertain tax positions together with the related liability in the balance sheet, and to include the expenses incurred related to such accruals in the provision for income taxes. There were no interest or penalties included in the provision for income taxes during the six months ended June 30, 2017 and 2016.

## NOTE 8—Commitments and Contingencies

## Leases

As of June 30, 2017, the Company leased eight facilities under operating lease arrangements. The lease expiration dates range from September 2019 to December 2025. Certain leases contain escalation clauses calling for increased rents. The Company recognizes rent expense on a straight-line basis over the lease period and has recorded deferred rent for the difference between rent payments and rent expense recognized.

## Legal Proceedings

From time to time, the Company is involved in litigation that it believes is of the type common to companies engaged in the Company's line of business, including commercial and employment disputes. As of the date of this Quarterly Report on Form 10-Q, the Company is not involved in any pending legal proceedings whose outcome the Company expects to have a material adverse effect on its financial position, results of operations or cash flows. However, litigation is unpredictable and excessive verdicts, both in the form of monetary damages and injunctions, could occur. In the future, litigation could result in substantial costs and diversion of resources, and the Company could incur judgments or enter into settlements of claims that could have a material adverse effect on its business.

## NOTE 9—Equity and Stock Incentive Plans

The Company recognized stock-based compensation expense related to awards granted under its 2009 Stock Option and Incentive Plan (the "2009 Plan"), 2011 Equity Incentive Award Plan (the "2011 Plan"), and ESPP.



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Total stock-based compensation expense recognized consisted of:

|                            | Three Months<br>ended June 30,<br>2017 |          | Six Months<br>ended June 30,<br>2016 |           |
|----------------------------|----------------------------------------|----------|--------------------------------------|-----------|
|                            | 2017                                   | 2016     | 2017                                 | 2016      |
|                            | (in thousands)                         |          |                                      |           |
| Cost of revenues           | \$ 1,675                               | \$ 1,132 | \$ 3,119                             | \$ 2,102  |
| Sales and marketing        | 1,258                                  | 1,059    | 2,434                                | 1,937     |
| Research and development   | 2,098                                  | 1,944    | 3,959                                | 3,448     |
| General and administrative | 3,479                                  | 3,883    | 6,849                                | 7,221     |
|                            | \$ 8,510                               | \$ 8,018 | \$ 16,361                            | \$ 14,708 |

2009 Stock Option and Incentive Plan and 2011 Equity Incentive Award Plan

Stock Options

The following table summarizes the Company's stock option activity under the 2009 Plan and 2011 Plan:

|                                                     | Number of<br>Shares | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term<br>(in years) | Aggregate<br>Intrinsic<br>Value<br>(in thousands) |
|-----------------------------------------------------|---------------------|------------------------------------------|-----------------------------------------------------------------------|---------------------------------------------------|
| Outstanding at January 1, 2017                      | 1,885,332           | \$ 26.21                                 | 6.34                                                                  | \$ 108,356                                        |
| Granted                                             | 6,601               | 94.66                                    |                                                                       |                                                   |
| Exercised                                           | (249,214 )          | 23.81                                    |                                                                       |                                                   |
| Forfeited or expired                                | (14,787 )           | 39.74                                    |                                                                       |                                                   |
| Outstanding at June 30, 2017                        | 1,627,932           | \$ 26.73                                 | 5.85                                                                  | \$ 135,413                                        |
| Ending vested and expected to vest at June 30, 2017 | 1,617,046           | \$ 26.59                                 | 5.84                                                                  | \$ 134,729                                        |
| Exercisable at June 30, 2017                        | 1,315,908           | \$ 22.78                                 | 5.48                                                                  | \$ 114,659                                        |

There were no stock options granted during the three months ended June 30, 2017. Stock options granted during the six months ended June 30, 2017 were made under the 2011 Plan. There were no grants under the 2009 Plan during the six months ended June 30, 2017.

The aggregate intrinsic value of the stock options outstanding at June 30, 2017 represents the value of the Company's closing stock price of \$109.91 on June 30, 2017 in excess of the exercise price multiplied by the number of options outstanding for options that were in-the-money. Options outstanding that are expected to vest are net of estimated future option forfeitures.

As of June 30, 2017, total unrecognized stock-based compensation expense related to unvested stock options, adjusted for estimated forfeitures, was \$6.1 million and is expected to be recognized over a weighted average period of 1.4 years.

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## Restricted Stock Units, Performance-Vesting Restricted Stock Units, and Performance Awards

The following table summarizes the Company's RSU, Performance Award and performance-vesting RSU activity:

|                                                     | RSUs                |                                                              | Performance Awards<br>and<br>Performance-Vesting<br>RSUs |                                                              |
|-----------------------------------------------------|---------------------|--------------------------------------------------------------|----------------------------------------------------------|--------------------------------------------------------------|
|                                                     | Number of<br>Shares | Weighted<br>Average<br>Grant Date<br>Fair Value<br>Per Share | Number of<br>Shares                                      | Weighted<br>Average<br>Grant Date<br>Fair Value<br>Per Share |
| Outstanding at January 1, 2017                      | 1,025,115           | \$ 64.47                                                     | 407,650                                                  | \$ 46.77                                                     |
| Granted                                             | 430,605             | 103.76                                                       | 41,201                                                   | 94.66                                                        |
| Released                                            | (275,361 )          | 54.91                                                        | (145,651 )                                               | 39.53                                                        |
| Forfeited or expired                                | (60,945 )           | 76.99                                                        | —                                                        | —                                                            |
| Outstanding at June 30, 2017                        | 1,119,414           | \$ 81.25                                                     | 303,200                                                  | \$ 56.76                                                     |
| Ending vested and expected to vest at June 30, 2017 | 967,205             |                                                              | 303,200                                                  |                                                              |

RSUs, performance-vesting RSUs and Performance Awards that are expected to vest are presented net of estimated future forfeitures. RSUs released during the six months ended June 30, 2017 and 2016 had an aggregate intrinsic value of \$29.2 million and \$14.6 million, respectively, and had an aggregate grant-date fair value of \$15.1 million and \$7.0 million, respectively. Performance-vesting RSUs and Performance Awards released during the six months ended June 30, 2017 and 2016 had an aggregate intrinsic value of \$13.7 million and \$9.3 million, respectively, and had an aggregate grant-date fair value of \$5.8 million and \$3.5 million, respectively. The number of RSUs released includes shares that the Company withheld on behalf of employees to satisfy the minimum statutory tax withholding requirements.

As of June 30, 2017, total unrecognized compensation expense related to unvested RSUs, performance-vesting RSUs and Performance Awards was \$77.2 million and is expected to be recognized over a weighted average period of 2.7 years.

**Employee Stock Purchase Plan**

For the six months ended June 30, 2017 and 2016, employees purchased 52,619 shares and 47,819 shares, respectively, under the ESPP for a total of \$4.3 million and \$2.9 million, respectively. As of June 30, 2017, unrecognized compensation expense related to the current semi-annual ESPP offering period, which ends on August 31, 2017, was \$0.5 million and is expected to be recognized over two months.

**Valuation Information**

The fair value of stock options and stock purchase rights granted under the 2009 Plan, the 2011 Plan, and the ESPP were estimated at the date of grant using the Black-Scholes option valuation model with the following weighted average assumptions:

|                                     | Three<br>months<br>ended<br>June 30,<br>2017 |      | Six Months<br>ended June<br>30,<br>2016 |        |
|-------------------------------------|----------------------------------------------|------|-----------------------------------------|--------|
|                                     | 2017                                         | 2016 | 2017                                    | 2016   |
| Stock option plans:                 |                                              |      |                                         |        |
| Risk-free interest rate             | %                                            | %    | 2.04 %                                  | 1.38 % |
| Expected life of options (in years) | —                                            | —    | 6.08                                    | 6.08   |
| Expected dividend yield             | %                                            | %    | — %                                     | — %    |
| Volatility                          | %                                            | %    | 48 %                                    | 47 %   |

**Employee Stock Purchase Plan:**

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|                                     |              |              |       |       |
|-------------------------------------|--------------|--------------|-------|-------|
| Risk-free interest rate             | <del>%</del> | <del>%</del> | 0.69% | 0.36% |
| Expected life of options (in years) | —            | —            | 0.50  | 0.50  |
| Expected dividend yield             | <del>%</del> | <del>%</del> | — %   | — %   |
| Volatility                          | <del>%</del> | <del>%</del> | 35 %  | 46 %  |

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## Common Stock

The following numbers of shares of common stock were reserved and available for future issuance at June 30, 2017:

|                                                         | Reserved<br>Shares |
|---------------------------------------------------------|--------------------|
| Options and awards outstanding under stock option plans | 3,050,546          |
| Shares available for future grant under the 2011 Plan   | 5,241,658          |
| Shares available under the ESPP                         | 1,683,080          |
| Total                                                   | 9,975,284          |

In February 2017, 336,856 additional shares were reserved under the ESPP, and 1,684,282 additional shares were reserved under the 2011 Plan, pursuant to the automatic increase provisions in each plan.

## Stock Repurchase Program

In May 2014, the Company's board of directors approved a stock repurchase program under which the Company is authorized to repurchase up to \$75.0 million of its common stock in which all shares are retired upon repurchase. This program ended in May 2017 and the Company did not repurchase any shares during the first five months of 2017.

## NOTE 10—Segment Information

The Company operates in one industry—mortgage-related software and services. The Company's chief operating decision maker is its chief executive officer, who makes decisions about resource allocation and reviews financial information presented on a consolidated basis. Accordingly, the Company has determined that it has a single reporting segment and operating unit structure, specifically, technology-enabled solutions to help streamline and automate the residential mortgage origination process for its network participants.

The Company is organized primarily on the basis of service lines. Supplemental disclosure of revenues by type is as follows:

|                     | Three months<br>ended June 30, |          | Six Months ended<br>June 30, |           |
|---------------------|--------------------------------|----------|------------------------------|-----------|
|                     | 2017                           | 2016     | 2017                         | 2016      |
|                     | (in thousands)                 |          |                              |           |
| On-demand revenues  | \$104,125                      | \$89,906 | \$197,127                    | \$163,005 |
| On-premise revenues | —                              | 192      | —                            | 718       |
|                     | \$104,125                      | \$90,098 | \$197,127                    | \$163,723 |

On-demand revenue is generated from company-hosted software subscriptions that customers access through the Internet. On-demand revenue is comprised of fees for software services sold both as a subscription and transactionally, including fees based on a per closed loan, or success basis, subject to monthly base fees, which the Company refers to as Success-Based Pricing; Ellie Mae Network fees; education and training, loan product, policy and guideline data and analytics services under the AllRegs brand; and professional services which include consulting, implementation, and training services.

On-premise revenue is generated from maintenance services, sales of customer-hosted Encompass software licenses, and related professional services. As of June 30, 2016, the Company completed the migration to its on-demand Encompass offering, and the Company does not expect to generate on-premise revenues in the future.

## ITEM 2—MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report on Form 10-Q and the documents incorporated herein by reference contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which are subject to the "safe harbor" created by those sections. These forward-looking statements include, but are not limited to, statements concerning our strategy, future operations, future financial performance, future revenues, future profitability, future products and services, projected costs, expectations regarding demand and acceptance of our products and services, growth opportunities, our reputation, future economic conditions, trends in the market in which we operate, the plans and objectives of management and the statements set forth in this Item 2 and the section captioned "Risk Factors" in this report.

Forward-looking statements may include words such as “may,” “will,” “should,” “expect,” “plan,” “intend,” “anticipate,” “believe,” “estimate,” “predict,” “potential,” “continue” or other wording indicating future results or expectations. Forward-looking statements are subject to risks and uncertainties, and actual events or results may differ materially. These forward-looking



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statements involve risks and uncertainties that could cause our actual results to differ materially from those described in the forward-looking statements, including, without limitation:

- outages and other system interruptions in our Encompass software, the Ellie Mae Network service or our other services and any related impact on our reputation;
- fluctuations in mortgage lending volume;
- the volume of mortgages originated by our Encompass users;
- the impact of changes in mortgage interest rates;
- changes in mortgage originator, lender, investor or service provider behavior and any related impact on the residential mortgage industry;
- our ability to accurately forecast revenues and appropriately plan our expenses;
- the number of Encompass users, including contracted Encompass users;
- the effectiveness of our marketing and sales efforts to attract new and retain existing Encompass users and Ellie Mae Network participants;
- transaction volume on the Ellie Mae Network;
- the level of demand for our Encompass Docs Solution, our Encompass Product & Pricing Service, our Encompass Compliance Service, our Encompass CRM service and the other services we offer;
- our ability to keep secure the confidential information of the customers of the users of our software and services;
- our ability to enhance the features and functionality of our software and services, including the development and successful deployment of our next generation Encompass platform;
- the timing of the introduction and acceptance of new software and services;
- changes in government regulation affecting mortgage lenders and Ellie Mae Network participants or our business, and potential structural changes in the U.S. residential mortgage industry;
  - customer retention, renewal and upgrade rates;
- the increased time, cost and complexity that may be required to successfully target larger customers;
- our ability to scale our operations and increase productivity to support our existing and growing customer base;
- our expected increase in investment in our products and services;
- our ability to successfully manage our growth and any future acquisitions of businesses, solutions or technologies;
- the risk that the anticipated benefits and growth prospects expected from our recent acquisitions may not be fully realized or may take longer to realize than expected;
- the timing of future acquisitions of businesses, solutions or technologies and new product launches;
- the impact of uncertain domestic and worldwide economic conditions, including the resulting effect on residential mortgage volumes;
- the attraction and retention of qualified employees and key personnel;
- our ability to compete effectively in a highly competitive market and adapt to technological changes;
- our ability to protect our intellectual property, including our proprietary Encompass software;
- costs associated with defending intellectual property infringement and other claims; our ability to maintain effective internal controls;
- the risk of natural and man-made catastrophic interruptions to our business; and
- the risks set forth in the section captioned “Risk Factors” in this report.

We do not assume any obligation to update any forward-looking statements, except as required by law.

In this report, references to “Ellie Mae,” the “Company,” “we,” “our” or “us” refer to Ellie Mae, Inc. together with its subsidiaries, unless the context requires otherwise.

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Overview

We are a leading provider of innovative on-demand software solutions and services for the residential mortgage industry in the United States. Banks, credit unions and mortgage lenders use our Encompass® all-in-one mortgage management solution to originate and fund mortgages and improve compliance, loan quality, and efficiency. Mortgage originators use our Encompass software, a comprehensive mortgage management system that handles key business and management functions involved in running a residential mortgage origination business. Mortgage originators use Encompass as a single tool for loan processing, marketing, and customer communication and to interact electronically with lenders, investors, and service providers over the Ellie Mae Network. Our software also enables enforcement of rules and business practices designed to ensure loan quality, adherence to processing standards and regulatory compliance.

The Ellie Mae Network electronically connects approximately 177,000 mortgage professionals using Encompass to the broad array of mortgage lenders, investors, and third-party service providers integral to the origination and funding of residential mortgages. During the mortgage origination process, mortgage originators may order various services through the Ellie Mae Network, including credit reports; product eligibility and pricing services; automated underwriting services; appraisals; title reports; insurance; flood certifications and flood insurance; compliance reviews; fraud detection; document preparation; and verification of income, identity, and employment. Mortgage originators can also initiate secure data transmission to and from lenders and investors.

On-demand revenues are generated primarily from subscriptions to the company-hosted Encompass Software that customers access through the Internet, including customers who pay fees based on the number of loans they close, or success basis, subject to monthly base fees, which we refer to as Success-Based Pricing, and related professional services such as consulting, implementation, and training services. On-demand revenues also include software related services that are sold on a transactional basis; Ellie Mae Network transaction fees paid by service providers, lenders, investors, and certain government-sponsored entities participating on the Ellie Mae Network; education and training; and loan product and guideline data and analytics services that are provided under the AllRegs brand. On-premise revenues are generated from customer-hosted software licenses and related professional services and maintenance services. As of June 30, 2016, we completed the migration of customers to our on-demand Encompass offering, and we do not expect to generate on-premise revenues in the future.

Our on-demand revenues typically, but not always, track the seasonality of the residential mortgage industry, with increased activity in the second and third quarters and reduced activity in the first and fourth quarters as home buyers tend to purchase their homes during the spring and summer in order to move to a new home before the start of the school year. Mortgage volumes are also impacted by other factors such as interest rate fluctuations, home sale activity, regulatory changes such as the TILA-RESPA Integrated Disclosure rule which became effective in October 2015, and general economic conditions, which can lead to departures from the typical seasonal pattern. During the first half of 2017, mortgage volumes declined relative to the first half of 2016 due to an increase in mortgage interest rates resulting in lower refinancings. This had the effect of reducing the number of closed loans per active user on our platform in the second quarter of 2017 relative to the same period in 2016. Although the market is expected to transition to one in which increasing volumes are driven primarily by demand for home purchases, a tight housing supply in certain markets is currently limiting the rate of growth in purchase volumes. As a result, closed loans per average active user on our platform are expected to continue to be lower in the second half of 2017 relative to the same period in 2016.

In spite of lower industry volume, we expect to increase revenue in 2017 and beyond through the use of our platform to both process an increasing percentage of loans originated in the United States, and to increase revenue earned per loan. This is achieved by the continued addition of new users, increasing productivity of our users through the use of Encompass and the increased adoption of our service offerings by our users.

We currently estimate that approximately 25% to 35% of our revenues have some direct sensitivity to volume. The base fee portion of success-based revenues, subscription revenues, and professional services revenues, are generally not affected by fluctuations in mortgage origination volume.

We are investing aggressively in initiatives that we believe will help us continue to grow our business, improve our products and services, and strengthen our competitive advantage while bringing sustainable long-term value to our

customers. Our recent launch of Developer Connect will enable developers to create new features for Encompass, easily integrate Encompass with external systems and data, and build and deploy custom applications in the cloud. We believe this open and simplified architecture will enable us to deploy add-on services more easily and drive significantly more revenue per loan. In addition, lenders are also looking for a technology partner to deliver a better digital mortgage experience to consumers. Here, our Consumer Connect solution allows lenders to provide better digital tools and a more easy-to-use web based experience as a seamless extension of Encompass.

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During 2016 and the first two quarters of 2017, we increased our investment in advancements to our platform, research and development, technology infrastructure, and data security to support our user additions, increased volumes of customer data and to maintain the confidentiality of our customers' data. This includes the rollout of our Connect solutions in the first half of 2017, the development of our hybrid cloud infrastructure to accommodate new users, and our next generation Encompass platform, which we expect to incrementally introduce in 2018. The amortization expense of capitalized costs associated with our Connect solutions decreased our gross margin percentage and increased operating expenses in the first six months of 2017 as compared to the same period in 2016. Conversely, capitalized costs associated with solutions that have not yet rolled out remain as an asset on our Condensed Consolidated Balance Sheet and reduced expense in the period they are capitalized.

We have also invested in our sales and client services capabilities to continue to increase sales of our products and to assist our customers in implementing our solutions. These investments include expanding our talent across the organization by hiring additional personnel. To continue to support customers as we grow our business and further differentiate ourselves, we intend to invest in key areas such as research and development, enterprise sales, services, technical support, data security, and data center infrastructure. We expect that our cost of revenues will continue to increase as our revenues increase, as we make additional and accelerated investments to bolster our infrastructure and enhance our system capacity, reliability, and data security, as we place new internal-use software into service, as we pursue additional strategic acquisitions, and as we continue to hire personnel in our implementation and customer support departments to support new customers and provide new services. As we continue to invest in these areas, such expenditures may affect our ability to improve our margins as we grow revenue.

In addition to our internal initiatives, our business strategy has evolved to address recent industry trends, including:

- greater focus on operational efficiencies;
- customers adopting multi-channel strategies;
- changes in regulation affecting lenders and investors;
- increased quality standards imposed by regulators, lenders, and investors; and
- greater focus by customers and regulators on data security and consumer privacy.

We are responding to these trends as follows:

Greater focus on operational efficiencies. The average total production cost per loan was \$8,887 in the first quarter of 2017<sup>1</sup>. We expect operational costs to continue to be a significant consideration for mortgage originators due to the continuously changing regulatory environment and heightened quality standards. By automating many of the functions of mortgage origination, we enable our users to comply with regulations and process quality loans more efficiently and effectively. This reduces the cost of originating loans and lowers the risk of buy-back demands from investors resulting from poorly originated or documented loans or loans that fail to comply with applicable regulations. We continually address the changing needs of our customers by developing and enhancing tools to allow for simplified regulatory compliance, increased availability of information, and enhanced system functionality and performance.

With an eye towards providing customers with ever-improving tools to enhance efficiency, we currently anticipate that we will continue to develop new service offerings through the Ellie Mae Network and pursue adoption of our services through initiatives such as our Encompass Connect Solutions. By integrating and expanding our current and new services, we aim to provide a more comprehensive solution to our users.

Customers adopting multi-channel strategies. Customers are developing multi-channel strategies beyond a single retail, correspondent or wholesale mortgage lending channel in order to grow their businesses. The requirements of these different channels vary and in order to maintain a single operating system, customers must use a robust system with customizable functionality. Encompass includes support for multi-channel workflows, allowing our customers to drive efficiencies and boost productivity by creating distinct workflows for each channel that map to our customers' business needs. Encompass users can customize workflows based on channel, loan purpose or specific loan criteria - all of which can vary between lending channels. With the introduction of Encompass TPO Connect, Encompass users will be able to utilize a customizable and interactive web experience for wholesale and correspondent lending channels, which gives lenders and investors a modern and collaborative web experience for their third-party

origination, or TPO, partners that promotes compliance, data integrity, and easy bi-directional communication throughout the entire loan process. Additionally, Encompass Consumer Connect enables our customers to originate loans directly from borrowers by offering an online loan application that can be accessed by anyone with a web browser.

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<sup>1</sup> Mortgage Bankers Association, Independent Mortgage Bank Volumes Decrease, Production Profits Drop in 1st Quarter 2017, June 6, 2017.

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Changes in regulation affecting lenders and investors. Regulations continue to be subject to change and many regulatory reforms have significantly increased the complexity and importance of regulatory compliance. We devote considerable resources to continually upgrade our software to help our customers address regulatory changes. We offer Encompass Compliance Service, which analyzes mortgage loan data for compliance with consumer protection laws and institutionally mandated compliance policies and also alerts users to possible violations of these laws and policies. In addition, we have a staff of attorneys who work with compliance experts and help ensure that documents prepared using our software and the processes recommended by the Encompass workflow comply with applicable rules and regulations. For example, additional tools and product updates were required to address the Ability-to-Repay/Qualified Mortgage and Federal and State High Cost rules that became effective in January 2014. In addition, we updated certain of our products to comply with the TILA-RESPA Integrated Disclosure rule changes that took effect in October 2015 and we will provide a complete offering of readiness initiatives, tools and training programs in advance of the 2018 Home Mortgage Disclosure Act and Regulation C (HMDA) collection and reporting changes. We believe we are well-positioned to help our customers comply with changing regulatory requirements as they are published and become effective. However, changes to existing laws or regulations or adoption of new laws or regulations relating to the residential mortgage industry could require us to incur significant costs to update our products and services so that our customers remain compliant with such laws and regulations.

Increased quality standards imposed by regulators, lenders and investors. Encompass is designed to automate and streamline the process of originating mortgages to, among other things, satisfy increased quality requirements of investors. Relevant features of Encompass include enabling customers' management to impose processing rules and formats, and providing milestone and process reminders, automated population of forms with accurate data, and accurate and automated transmission of loan files and data from originators to investors and lenders. Our TQL program is designed to further enhance the quality, compliance, and salability of loans that are originated through Encompass. Additionally, TQL is intended to reduce the possibility of errors in the process of transferring information from originator to investor and to give investors confidence in the accuracy and regulatory compliance of the information that is underlying loan files.

In response to the increased quality standards and compliance mandates affecting the industry, we expect many non-Encompass mortgage lenders to assess new platform options and replace their legacy systems. We have increased the size of our customer acquisition, implementation, and support teams in order to address anticipated demand for our software solutions.

Greater focus by customers and regulators on data security and consumer privacy. Recent high-profile data security incidents affecting banking institutions and cloud-service software providers have resulted in an increased focus on data security by our customers and our customers' regulators. We are making significant investments in the security of the Encompass service, as well as our internal systems, processes and monitoring capabilities to protect our customers' data and help minimize the risk of data security loss. We expect the industry focus on data security to continue to increase, and we anticipate that our investments in data security will increase substantially over time.

### Acquisition Strategy

Our industry is highly fragmented, and we are evaluating strategic opportunities available to acquire technology-based companies that will complement and increase the attractiveness of our solutions. In October 2015, for example, we acquired substantially all of the assets of Mortgage Returns, LLC, a company that provides on-demand customer relationship management, or CRM, and marketing automation solutions for the residential mortgage industry. With the acquisition of Mortgage Returns, we are responding to the needs of our customers by adding a robust CRM solution for lenders of all sizes. We believe such acquisitions enhance our product and service offerings and further our mission of automating the entire end-to-end mortgage process for our customers.

### Operating Metrics

We use certain operational metrics to evaluate our business, determine allocation of our resources, and make decisions regarding corporate strategy. We focus on these metrics to determine our success in leveraging our user base to increase our revenues and to gauge the degree of our market penetration.

These metrics are defined below.

Contracted revenues. Contracted revenues are those revenues that are fixed by the terms of a contract and are generally not affected by fluctuations in mortgage origination volume. These revenues consist of the base fee portion of success-based revenues, monthly per-user subscription revenues, professional services revenues, and subscription revenues paid for products other than Encompass.

Active users. An active user is a mortgage origination professional who has used Encompass at least once within a 90-day period preceding the measurement date. A user is a mortgage origination professional working at an Encompass mortgage lender, such as a mortgage bank, commercial bank, thrift or credit union, which sources and funds loans and generally sells these funded loans to investors; or a mortgage brokerage, which typically processes and submits loan files to a mortgage lender or mega lender that funds the loan.

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Contracted users. A contracted user is a mortgage origination professional who has a license to use Encompass and has an obligation to pay for this license, but who is not necessarily an active user.

Average active users. Average active users during a period is calculated by averaging the monthly active users during a reporting period.

Revenue per average active Encompass user. Revenue per average active Encompass user is calculated by dividing total revenues by average active Encompass users.

The following table shows these operating metrics as of and for the three and six months ended June 30, 2017 and 2016:

|                                                   | Three Months ended<br>June 30, |           | Six Months ended June<br>30, |            |
|---------------------------------------------------|--------------------------------|-----------|------------------------------|------------|
|                                                   | 2017                           | 2016      | 2017                         | 2016       |
| Revenues (in thousands):                          |                                |           |                              |            |
| Total revenues                                    | \$ 104,125                     | \$ 90,098 | \$ 197,127                   | \$ 163,723 |
| Total contracted revenues                         | \$ 67,106                      | \$ 49,582 | \$ 129,964                   | \$ 95,538  |
| Users at end of period:                           |                                |           |                              |            |
| Contracted users                                  | 231,919                        | 192,980   | 231,919                      | 192,980    |
| Active users                                      | 177,366                        | 153,334   | 177,366                      | 153,334    |
| Active users as a percentage of contracted users  | 76                             | % 79      | % 76                         | % 79       |
| Average active users:                             |                                |           |                              |            |
| Average active users during the period            | 175,266                        | 149,876   | 172,021                      | 145,478    |
| Revenue per average active user during the period | \$ 594                         | \$ 601    | \$ 1,146                     | \$ 1,125   |

**Basis of Presentation****General**

Our consolidated financial statements include the accounts of Ellie Mae, Inc. and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated upon consolidation.

**Revenue Recognition**

We generate revenues primarily from subscription services and usage-based fees, transaction-based fees, and fees from professional services. We categorize our revenue as on-demand and on-premise (prior to May 1, 2016). Sales taxes assessed by governmental authorities are excluded from revenue.

**On-demand Revenue**

On-demand revenue is generated from the company-hosted Encompass Software subscriptions that customers access through the Internet. On-demand revenue is comprised of fees for software services sold both as a subscription and transactionally, including fees based on a per closed loan, or success basis, subject to monthly base fees, which we refer to as Success-Based Pricing; Ellie Mae Network fees; education and training, loan product, policy and guideline data and analytics services under the AllRegs brand; and professional services which include consulting, implementation, and training services.

**On-premise Revenue**

On-premise revenue is generated from maintenance services, sales of customer-hosted Encompass software licenses, and related professional services. As of June 30, 2016, we completed the migration of customers to our on-demand Encompass offering, and we do not expect to generate on-premise revenues in the future.

**Cost of Revenues and Operating Expenses****Cost of Revenues**

Our cost of revenues consists primarily of: salaries and benefits, including stock-based compensation expense; data center operating costs; depreciation on data center computer equipment; amortization of internal-use software and acquired intangible assets such as developed technology and trade names; customer support; professional services associated with implementation of our software; third-party royalty expenses; and allocated facilities costs. We expect that our cost of revenues will continue to





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increase in absolute dollars as our revenues increase, as we make additional and accelerated investments to bolster our infrastructure and enhance our system capacity, reliability, and data security, as we place new internal-use software into service, as we pursue additional strategic acquisitions, and as we continue to hire personnel in our implementation and customer support departments to support new customers and provide new services. We anticipate that we will continue to invest in key areas such as internal-use software, our services, technical support, data security, and data center infrastructure to better support our customers and further differentiate ourselves. This will include development of our next generation Encompass platform, which we expect to place into service during 2018.

### Sales and Marketing

Our sales and marketing expenses consist primarily of: salaries, benefits, and incentive compensation, including stock-based compensation expense and commissions; allocated facilities costs; expenses for trade shows, public relations, our annual user conference, and other promotional and marketing activities; expenses for travel and entertainment; and amortization of acquired intangible assets such as customer relationships. We expect that our sales and marketing expenses will continue to increase as we hire additional sales personnel in order to address anticipated demand for our software solutions, as we pursue additional strategic acquisitions and as our annual user conference continues to increase in size. We also intend to increase marketing activities focused on our Encompass Lending Platform, our Ellie Mae Network offerings, and our other Encompass services.

### Research and Development

Our research and development expenses consist primarily of: salaries and benefits, including bonuses and stock-based compensation expense; fees to contractors engaged in the development of the Encompass software, Ellie Mae Network, and other products; and allocated facilities costs. We expect that our research and development expenses will continue to increase in absolute dollars as we continue to invest in our products and services and related next-generation enhancements, including hiring additional engineering and product development personnel and as we pursue additional strategic acquisitions.

### General and Administrative

Our general and administrative expenses consist primarily of: salaries and benefits, including bonuses and stock-based compensation expense for employees involved in finance, accounting, human resources, administration, information technology, and legal; third-party provider expenses such as general consulting, legal, accounting, and other professional services; and allocated facilities costs. We expect general and administrative expenses to continue to increase in absolute dollars as we expand our facilities and invest in our back office infrastructure to enhance our system capacity, reliability and security. We also expect general and administrative expenses to continue to increase as we hire additional personnel and grant stock-based awards to attract and retain the employees needed to continue to grow our business and as we pursue additional strategic acquisitions.

### Other Income, Net

Other income, net consists of interest income earned on investments and cash accounts, offset by investment discount amortization, and interest expense paid on equipment and software leases.

### Income Taxes

On a quarterly basis, we evaluate our expected income tax expense or benefit based on our year-to-date operations, and we record an adjustment in the current quarter. The net tax provision is the result of the mix of profits earned by us and our subsidiaries in tax jurisdictions with a broad range of income tax rates. We are required to estimate deferred tax assets and liabilities based on the differences between the financial reporting and tax bases of assets and liabilities measured using the enacted tax rates that will be in effect when the differences are expected to reverse. In general, deferred tax assets represent future tax benefits to be received when certain expenses previously recognized in our consolidated statements of operations become deductible expenses under applicable income tax laws or loss or credit carry forwards are utilized. Accordingly, realization of our deferred tax assets is dependent on future taxable income against which these deductions, losses, and credits can be utilized. Management uses judgment to assess the likelihood that our deferred tax assets will be recovered from future taxable income and to the extent we believe that recovery is not more likely than not, we must establish a valuation allowance to reduce the deferred tax assets to the amount that is more likely than not to be realized. We adopted ASU 2016-09 as of January 1, 2017. As a result of the adoption, excess tax benefits are recognized as income tax benefit or expense when stock awards vest or are settled,

which reduced our effective tax rate for the first half of 2017. Given the inherent uncertainty in predicting future share-based transactions, actual benefits realized may vary, and may result in volatility to our income tax expense or benefit.

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## Critical Accounting Policies and Estimates

There have been no material changes during the three and six months ended June 30, 2017 to our critical accounting policies and estimates previously disclosed in our 2016 Form 10-K except in relation to our adoption of ASU No. 2016-09, Compensation—Stock Compensation (Topic 718): Improvements to Employee Shared-Based Payment Accounting on January 1, 2017, whereby we now record excess tax benefits and tax deficiencies as income tax benefit or expense when stock awards vest or settle, and we no longer classify the cash flow from excess tax benefits as a reduction from operating cash flows. This resulted in a \$1.2 million increase in net cash provided by operating activities and a corresponding \$1.2 million decrease in net cash provided by financing activities for the six months ended June 30, 2016.

## Results of Operations

The following tables set forth our results of operations for the periods presented and as a percentage of our revenues for those periods. The period-to-period comparison of financial results is not necessarily indicative of future results.

|                                           | Three Months<br>ended June 30, |          | Six Months ended<br>June 30, |           |
|-------------------------------------------|--------------------------------|----------|------------------------------|-----------|
|                                           | 2017                           | 2016     | 2017                         | 2016      |
|                                           | (in thousands)                 |          |                              |           |
| Revenues                                  | \$104,125                      | \$90,098 | \$197,127                    | \$163,723 |
| Cost of revenues <sup>(1)</sup>           | 38,267                         | 28,453   | 73,035                       | 55,084    |
| Gross profit                              | 65,858                         | 61,645   | 124,092                      | 108,639   |
| Operating expenses:                       |                                |          |                              |           |
| Sales and marketing <sup>(1)</sup>        | 13,860                         | 12,506   | 33,240                       | 27,792    |
| Research and development <sup>(1)</sup>   | 16,046                         | 14,662   | 33,453                       | 27,115    |
| General and administrative <sup>(1)</sup> | 18,727                         | 17,793   | 35,669                       | 33,525    |
| Total operating expenses                  | 48,633                         | 44,961   | 102,362                      | 88,432    |
| Income from operations                    | 17,225                         | 16,684   | 21,730                       | 20,207    |
| Other income, net                         | 762                            | 162      | 1,263                        | 361       |
| Income before income taxes                | 17,987                         | 16,846   | 22,993                       | 20,568    |
| Income tax provision (benefit)            | (836)                          | ) 6,258  | (5,429)                      | ) 7,474   |
| Net income                                | \$18,823                       | \$10,588 | \$28,422                     | \$13,094  |

<sup>(1)</sup> Stock-based compensation included in the above line items:

|                            | Three Months<br>ended June 30, |         | Six Months<br>ended June 30, |          |
|----------------------------|--------------------------------|---------|------------------------------|----------|
|                            | 2017                           | 2016    | 2017                         | 2016     |
|                            | (in thousands)                 |         |                              |          |
| Cost of revenues           | \$1,675                        | \$1,132 | \$3,119                      | \$2,102  |
| Sales and marketing        | 1,258                          | 1,059   | 2,434                        | 1,937    |
| Research and development   | 2,098                          | 1,944   | 3,959                        | 3,448    |
| General and administrative | 3,479                          | 3,883   | 6,849                        | 7,221    |
|                            | \$8,510                        | \$8,018 | \$16,361                     | \$14,708 |

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|                                       | Three Months<br>ended June 30,<br>2017 |        | Six Months<br>ended June 30,<br>2016 |        |
|---------------------------------------|----------------------------------------|--------|--------------------------------------|--------|
| Revenues                              | 100.0 %                                | 100.0% | 100.0 %                              | 100.0% |
| Cost of revenues                      | 36.7                                   | 31.6   | 37.0                                 | 33.6   |
| Gross profit                          | 63.3                                   | 68.4   | 63.0                                 | 66.4   |
| Operating expenses:                   |                                        |        |                                      |        |
| Sales and marketing                   | 13.3                                   | 13.9   | 16.9                                 | 17.0   |
| Research and development              | 15.4                                   | 16.3   | 17.0                                 | 16.6   |
| General and administrative            | 18.0                                   | 19.7   | 18.1                                 | 20.4   |
| Total operating expenses              | 46.7                                   | 49.9   | 52.0                                 | 54.0   |
| Income from operations                | 16.6                                   | 18.5   | 11.0                                 | 12.4   |
| Other income, net                     | 0.7                                    | 0.2    | 0.6                                  | 0.2    |
| Income before income taxes            | 17.3                                   | 18.7   | 11.6                                 | 12.6   |
| Income tax provision (benefit) (0.8 ) | 6.9                                    | (2.8 ) | 4.6                                  |        |
| Net income                            | 18.1 %                                 | 11.8 % | 14.4 %                               | 8.0 %  |

Comparison of the Three and Six Months Ended June 30, 2017 and 2016

## Revenues

The following table sets forth our revenues by type for the periods presented:

|                  | Three Months ended<br>June 30,<br>2017 |          | Six Months ended June<br>30,<br>2016 |           |
|------------------|----------------------------------------|----------|--------------------------------------|-----------|
|                  | 2017                                   | 2016     | 2017                                 | 2016      |
|                  | (dollars in thousands)                 |          |                                      |           |
| Revenue by type: |                                        |          |                                      |           |
| On-demand        | \$104,125                              | \$89,906 | \$197,127                            | \$163,005 |
| On-premise       | —                                      | 192      | —                                    | 718       |
| Total            | \$104,125                              | \$90,098 | \$197,127                            | \$163,723 |

|                  | Three Months ended<br>June 30,<br>2017 |         | Six Months ended June<br>30,<br>2016 |         |
|------------------|----------------------------------------|---------|--------------------------------------|---------|
|                  | 2017                                   | 2016    | 2017                                 | 2016    |
| Revenue by type: |                                        |         |                                      |         |
| On-demand        | 100.0 %                                | 99.8 %  | 100.0 %                              | 99.6 %  |
| On-premise       | — %                                    | 0.2 %   | — %                                  | 0.4 %   |
| Total            | 100.0 %                                | 100.0 % | 100.0 %                              | 100.0 % |

Three months ended June 30, 2017. Total revenues increased \$14.0 million, or 15.6%, for the three months ended June 30, 2017 as compared to the same period in 2016.

On-demand revenues increased by \$14.2 million, or 15.8% during the three months ended June 30, 2017, primarily due to a 20.2% increase in contracted users as of June 30, 2017 compared to the same period in 2016, partially offset by lower mortgage origination volumes driven mainly by an industrywide decrease in refinancings due to higher interest rates. The increase in contracted users resulted in a \$9.6 million increase in Encompass revenue mainly attributable to a \$12.6 million, or 35.2%, increase in base fees, partially offset by a decrease of \$3.0 million in additional closed loan fees, which are assessed for loans closed in excess of base fees under our Success-Based Pricing model. Significantly lower refinance origination volumes had the effect of reducing closed loans per average active user in the second quarter of 2017 as compared to same quarter in 2016 resulting in a reduction in revenue per average active user.

The implementation of new users and increased use of training other technical support offerings also contributed to a \$3.7 million increase in revenues from professional services, and we had a \$0.6 million increase in network revenues

from increased usage of third-party providers of services needed to process loans.

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We did not generate any on-premise revenues in the three months ended June 30, 2017 compared to \$0.2 million in the same period in 2016, primarily due to the completion of all on-premise customers' migration to our on-demand Encompass offering. We do not expect to generate on-premise revenues in the future.

Six months ended June 30, 2017. Total revenues increased \$33.4 million, or 20.4%, for the six months ended June 30, 2017 as compared to the same period of 2016.

On-demand revenues increased by \$34.1 million, or 20.9%, during the six months ended June 30, 2017, primarily due to a 20.2% increase in contracted users as of June 30, 2017 compared to the same period in 2016, partially offset by lower mortgage origination volumes driven mainly by an industrywide decrease in refinancings due to higher interest rates. The increase in contracted users resulted in a \$22.3 million increase in Encompass revenue mainly attributable to a \$26.5 million, or 39.2%, increase in base fees, partially offset by a decrease of \$4.2 million in additional closed loan fees, which are assessed for loans closed in excess of base fees under our Success-Based Pricing model.

The implementation of new users and increased use of training other technical support offerings also contributed to a \$7.8 million increase in revenues from professional services. We also had a \$3.3 million increase in revenues from other software and services due to increased usage by Encompass users, and a \$1.5 million increase in network revenues from increased usage of third-party providers of services needed to process loans.

We did not generate on-premise revenues in the six months ended June 30, 2017 compared to \$0.7 million in the same period in 2016, primarily due to the completion of all on-premise customers' migration to our on-demand Encompass offering, and we do not expect to generate on-premise revenues in the future.

## Gross Profit

|              | Three Months ended     |          | Six Months ended June |           |
|--------------|------------------------|----------|-----------------------|-----------|
|              | June 30,               |          | 30,                   |           |
|              | 2017                   | 2016     | 2017                  | 2016      |
|              | (dollars in thousands) |          |                       |           |
| Gross profit | \$65,858               | \$61,645 | \$124,092             | \$108,639 |
| Gross margin | 63.3                   | % 68.4   | % 63.0                | % 66.4    |

Gross profit increased by \$4.2 million and gross margin percentage decreased by 5.1% during the three months ended June 30, 2017 as compared to the same period in 2016. Revenues increased by \$14.0 million and cost of revenues increased by \$9.8 million. The decrease in the gross margin percentage was the result of a higher increase in cost relative to the increase in revenue. The increase in cost primarily include a \$4.1 million increase in amortization expense related to internal-use software and depreciation expense related to infrastructure hardware placed into service, a \$2.9 million increase in salaries, employee benefits, and stock-based compensation expenses associated with additional headcount for our professional services and customer support organizations in anticipation of continued increasing demand for our software solutions, a \$1.8 million increase in third-party royalty expenses arising from the increased revenues, and a \$1.1 million increase in expenses related to upgrades and services to our data centers hardware and technology as we increase capacity relating to new customers through our hybrid cloud architecture. Gross profit increased by \$15.5 million and gross margin percentage decreased by 3.4% during the six months ended June 30, 2017 as compared to the same period in 2016. Revenues increased by \$33.4 million and cost of revenues increased by \$18.0 million. The decrease in the gross margin percentage was the result of a higher increase in cost relative to the increase in revenues. The increase in cost primarily includes a \$7.5 million increase in amortization expense related to internal-use software and depreciation expense related to infrastructure hardware placed into service, a \$6.2 million increase in salaries, employee benefits, and stock-based compensation expenses associated with increased headcount in our professional services and customer support organizations in anticipation of continued increasing demand for our software solutions, a \$2.7 million increase in third-party royalty expenses arising from the increased revenues, and a \$2.2 million increase in expenses related to upgrades and services to our data centers hardware and technology as we increase capacity related to new customers.

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## Sales and Marketing

|                                        | Three Months ended<br>June 30, |          | Six Months ended<br>June 30, |          |   |
|----------------------------------------|--------------------------------|----------|------------------------------|----------|---|
|                                        | 2017                           | 2016     | 2017                         | 2016     |   |
|                                        | (dollars in thousands)         |          |                              |          |   |
| Sales and marketing                    | \$13,860                       | \$12,506 | \$33,240                     | \$27,792 |   |
| Sales and marketing as a % of revenues | 13.3                           | % 13.9   | % 16.9                       | % 17.0   | % |

Sales and marketing expenses increased by \$1.4 million, or 10.8%, for the three months ended June 30, 2017 as compared to the same period in 2016. Sales and marketing expenses as a percentage of revenues decreased by 0.6%. The increase in sales and marketing expenses was primarily due to a \$1.5 million increase in salaries, employee benefits, and stock-based compensation expenses related to increased headcount as we continue to grow our sales and marketing department in an effort to increase our market share and address anticipated demand for our software solutions.

Sales and marketing expenses increased by \$5.4 million, or 19.6%, for the six months ended June 30, 2017 as compared to the same period in 2016. Sales and marketing expenses as a percentage of revenues remained relatively flat. The increase in sales and marketing expenses were primarily due to a \$3.1 million increase in salaries, employee benefits, and stock-based compensation expenses related to increased headcount as we continue to grow our sales and marketing department in an effort to increase our market share and address anticipated demand for our software solutions, a \$1.1 million increase in marketing and promotion expenses including our user conference, and a \$0.2 million increase in commissions paid to our sales representatives arising from the increased bookings.

## Research and Development

|                                             | Three Months ended<br>June 30, |          | Six Months ended<br>June 30, |          |   |
|---------------------------------------------|--------------------------------|----------|------------------------------|----------|---|
|                                             | 2017                           | 2016     | 2017                         | 2016     |   |
|                                             | (dollars in thousands)         |          |                              |          |   |
| Research and development                    | \$16,046                       | \$14,662 | \$33,453                     | \$27,115 |   |
| Research and development as a % of revenues | 15.4                           | % 16.3   | % 17.0                       | % 16.6   | % |

Research and development expenses increased by \$1.4 million, or 9.4%, for the three months ended June 30, 2017 as compared to the same period in 2016. Research and development expenses as a percentage of revenues decreased by 0.9%. The increase in research and development expenses were primarily driven by salaries, employee benefits, and stock-based compensation expenses related to increased headcount and fees to contractors as we continue to invest in our products and services.

Research and development expenses increased by \$6.3 million, or 23.4%, for the six months ended June 30, 2017 compared to the same period in 2016. Research and development expenses as a percentage of revenues increased by 0.4%. The increase in research and development expenses were primarily driven by salaries, employee benefits, and stock-based compensation expenses related to increased headcount and fees to contractors as we continue to invest in our products and services.

## General and Administrative

|                                               | Three Months ended<br>June 30, |          | Six Months ended<br>June 30, |          |   |
|-----------------------------------------------|--------------------------------|----------|------------------------------|----------|---|
|                                               | 2017                           | 2016     | 2017                         | 2016     |   |
|                                               | (dollars in thousands)         |          |                              |          |   |
| General and administrative                    | \$18,727                       | \$17,793 | \$35,669                     | \$33,525 |   |
| General and administrative as a % of revenues | 18.0                           | % 19.7   | % 18.1                       | % 20.4   | % |

General and administrative expenses increased by \$0.9 million, or 5.2%, for the three months ended June 30, 2017 as compared to the same period in 2016. General and administrative expenses as a percentage of revenues decreased by 1.7%. The increase in general and administrative expenses was primarily due to a \$0.6 million increase in third-party consulting services, and a \$0.2 million increase in salaries, stock-based compensation, and employee benefits related to increased headcount.



General and administrative expenses increased by \$2.1 million, or 6.4%, for the six months ended June 30, 2017 as compared to the same period in 2016. General and administrative expenses as a percentage of revenues decreased by 2.3%. The increase in general and administrative expenses were primarily due to a \$1.7 million increase in salaries, stock-based compensation, and employee benefits related to increased headcount.

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## Income Tax Provision

|                                   | Three Months<br>ended June 30, |         | Six Months ended<br>June 30, |         |
|-----------------------------------|--------------------------------|---------|------------------------------|---------|
|                                   | 2017                           | 2016    | 2017                         | 2016    |
|                                   | (dollars in thousands)         |         |                              |         |
| Income tax provision (benefit)    | \$(836)                        | \$6,258 | \$(5,429)                    | \$7,474 |
| Effective tax rate <sup>(1)</sup> | (4.7 )%                        | 37.2 %  | (23.6 )%                     | 36.3 %  |

<sup>(1)</sup> Adoption of ASU 2016-09 resulted in a favorable effective tax rate impact of 40.9% and 60.1% for the three and six months ended June 30, 2017, respectively.

Income tax provision was a benefit of \$0.8 million for the three months ended June 30, 2017, compared to an expense of \$6.3 million for the three months ended June 30, 2016. The decrease in income tax provision was primarily due to the inclusion of excess tax benefits from stock based awards as a benefit in the income statement due to the adoption of ASU 2016-09. For further details regarding the adoption of ASU 2016-09, please refer to Note 2 of the Notes to Condensed Consolidated Financial Statements.

Income tax provision was a benefit of \$5.4 million for the six months ended June 30, 2017, compared to an expense of \$7.5 million for the six months ended June 30, 2016. The decrease in income tax provision and the effective tax rate for the six months ended June 30, 2017 was primarily due to the inclusion of excess tax benefits from stock based awards as a benefit in the income statement due to the adoption of ASU 2016-09. For further details regarding the adoption of ASU 2016-09, please refer to Note 2 of the Notes to Condensed Consolidated Financial Statements.

## Liquidity and Capital Resources

As of June 30, 2017, we had cash, cash equivalents, and short-term investments of \$333.7 million and long-term investments of \$121.1 million. This balance reflects cash proceeds of approximately \$271.4 million from the public offering completed in August 2016 of 3,162,500 shares of common stock, net of underwriting discounts, and offering costs and expenses. Cash and cash equivalents consist of cash, money market accounts, and highly liquid investments purchased with an original maturity of three months or less. Both short and long-term investments consist of U.S. government notes, and U.S. government agency securities, corporate bonds and obligations, certificates of deposit and municipal obligations.

We believe that our existing cash, cash equivalents, and short-term investments will be sufficient to fund capital expenditures, operating expenses and other cash requirements for at least the next 12 months. We may use our cash and investments to repurchase our stock. We may enter into acquisitions in the future, which could be funded by our cash and investments or require us to seek additional equity or debt financing. Additional funds may not be available on terms favorable to us or at all.

The following table sets forth our statement of cash flows data for the periods presented:

|                                                      | Six Months ended<br>June 30, |           | Net         |
|------------------------------------------------------|------------------------------|-----------|-------------|
|                                                      | 2017                         | 2016      | Change      |
|                                                      | (in thousands)               |           |             |
| Net cash provided by operating activities            | \$35,021                     | \$23,206  | 11,815      |
| Net cash used in investing activities                | (200,962 )                   | (16,003 ) | (184,959 )  |
| Net cash provided by (used in) financing activities  | (1,762 )                     | 3,010     | (4,772 )    |
| Net increase (decrease) in cash and cash equivalents | \$(167,703)                  | \$10,213  | \$(177,916) |

## Operating Activities

Cash provided by operating activities for the six months ended June 30, 2017 increased by \$11.8 million as compared to the same period in 2016. In the condensed consolidated statements of cash flows, cash provided by operating activities is presented as net income adjusted for non-cash items and changes in operating assets and liabilities. Net income increased by \$15.3 million for the six months ended June 30, 2017 as compared to the same period in 2016. Non-cash items resulted in a net decrease in cash from operations of \$4.0 million for the six months ended June 30, 2017 as compared to the same period in 2016. Changes in operating assets and liabilities resulted in a net increase in

cash from operations of \$0.5 million for the six months ended June 30, 2017 as compared to the same period in 2016. The \$4.0 million decrease in the net contribution of non-cash items to cash provided by operating activities was primarily due to a \$7.6 million increase in depreciation/amortization expense from data center equipment, internal-use software, leasehold

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improvements, and furniture and fixtures placed into service and a \$1.7 million increase in stock-based compensation expense due to increased headcount, partially offset by a \$11.8 million decrease in cash flow due to the increase in deferred tax assets.

Changes in operating assets and liabilities resulted in a net increase of \$0.5 million to cash provided by operating activities for the six months ended June 30, 2017 as compared to the same period in 2016. Our net accounts receivable balance fluctuates from period to period, depending on the amount and timing of sales and billing activity, our customers' payment method, and cash collections. Additionally, we experienced overall growth in our accounts receivable balance due to increased revenue for the six months ended June 30, 2017 as compared to the same period in 2016. The change in prepaid expenses and other current assets was primarily due to the timing of payments for software services and other maintenance. The change in accounts payable and accrued and other liabilities was primarily due to the annual payment of variable compensation costs in March 2017 as well as the timing of additional liabilities and payments in general, and does not reflect any significant change in the nature of accrued liabilities. The decrease in deferred revenue is primarily the result of timing of customer payments and the completion of professional services projects.

**Investing Activities**

Our primary investing activities have consisted of purchases and maturities of investments, and purchases of property and equipment (including costs incurred to develop internal-use software). Purchases of property and equipment may vary from period to period due to the timing of the expansion of our operations and the timing of our internal-use software projects subject to capitalization. We plan to continue to invest in the expansion of our operations and facilities as well as the next generation Encompass platform, and we intend to continue pursuing strategic acquisitions. Cash used in investing activities of \$201.0 million for the six months ended June 30, 2017 was primarily the result of \$21.8 million in expenditures for purchases of property, including capital improvements to our new corporate headquarters, investments to bolster our infrastructure and enhance our system capacity, reliability, and security, and \$25.5 million in expenditures incurred to develop internal-use software and website applications, including the development of our next generation Encompass platform. We also incurred \$153.7 million in net purchases of investments.

Cash used in investing activities of \$16.0 million for the six months ended June 30, 2016 was primarily the result of \$15.6 million in expenditures for purchases of property, including capital improvements to our new corporate headquarters, investments to bolster our infrastructure and enhance our system capacity, reliability, and security, and \$16.4 million expenditures incurred to develop internal-use software and website applications, including the development of our next generation Encompass platform. Additionally, we sold net \$15.9 million of investments to fund these expenditures.

**Financing Activities**

Financing activities have consisted primarily of cash provided from the exercise of stock options and purchases under the employee stock purchase plan, reduced by the payments related to capital lease obligations, repurchases of common stock and tax payments related to shares withheld for vested restricted stock units, or RSUs. In August 2016, we completed a public offering of common stock and sold a total of 3,162,500 shares of our common stock for total cash proceeds of approximately \$271.4 million, net of underwriting discounts, and offering costs and expenses of approximately \$13.2 million, which will be used for general corporate purposes, including working capital, sales and marketing activities, general and administrative matters and capital expenditures, and we may also use the net proceeds for the acquisition of, or investment in, technologies, solutions or businesses that complement our business. In May 2014, our board of directors approved a stock repurchase program under which we are authorized to repurchase up to \$75.0 million of our common stock over a 36-month period. This program ended in May 2017 and the Company did not repurchase any shares during the first five months of 2017.

Cash used in financing activities of \$1.8 million for the six months ended June 30, 2017 consisted primarily of \$11.4 million in tax payments related to shares withheld for vested RSUs, partially offset by \$10.2 million in proceeds from employee stock purchases and the exercise of stock options.

Cash provided by financing activities of \$3.0 million for the six months ended June 30, 2016 consisted primarily of \$9.1 million in proceeds from employee stock purchases and the exercise of stock options, partially offset by \$6.1

million in payments on capital leases and tax payments related to shares withheld for vested RSUs.

Off Balance Sheet Arrangements

As of June 30, 2017, we had no off-balance sheet arrangements, and operating leases were the only financing arrangements not reported on our condensed consolidated financial statements.

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Contractual Obligations

During the six months ended June 30, 2017, there have been no material changes to our contractual obligations outside the ordinary course of business from those specified in the 2016 Form 10-K.

ITEM 3—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We believe that there have been no significant changes in our market risk exposures for the three and six months ended June 30, 2017, as compared with those discussed in our 2016 Form 10-K.

ITEM 4—CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2017. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of June 30, 2017, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at a reasonable assurance level.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II—OTHER INFORMATION

ITEM 1—LEGAL PROCEEDINGS

For a description of the material legal proceedings, please see Note 8 of the Notes to Condensed Consolidated Financial Statements.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below and the other information in this report. If any of the following risks materialize, our business could be materially harmed, and our financial condition and results of operations could be materially and adversely affected. The risks described below are not the only ones facing us. Additional risks not currently known to us or that we currently believe are immaterial may also impair our business, results of operations, financial condition, and liquidity.

The following discussion of risk factors contains forward-looking statements. These risk factors may be important to understanding other statements in this Quarterly Report on Form 10-Q. The following information should be read in conjunction with the condensed consolidated financial statements and related notes in Part I, Item 1, “Financial Statements” and Part I, Item 2, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this Quarterly Report on Form 10-Q.

Because of the following risks, as well as other factors affecting our financial condition and operating results, past financial performance should not be considered to be a reliable indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods.

Any future outages or system interruptions that impair access to Encompass, the Ellie Mae Network or our other services could damage our reputation and brand and may substantially harm our business and operating results. The satisfactory performance, reliability, and availability of Encompass, the Ellie Mae Network and our other services are critical to our reputation and our ability to attract and retain Encompass users and Ellie Mae Network participants. Because our services are complex and incorporate a variety of hardware and proprietary and third-party software, our services may have errors or defects that could result in unanticipated downtime for our customers. Internet-based services frequently contain undetected errors when first introduced or when new versions or enhancements are released, and we have from time to time found errors and defects in our services and new errors and defects in our services may be detected in the future.

Moreover, we have experienced and may in the future continue to experience temporary system interruptions to Encompass, the Ellie Mae Network, or our other services for a variety of other reasons, including network failures, power failures, problems with Encompass and other third-party firmware updates, as well as an overwhelming number of users or Ellie Mae Network participants trying to access our services during periods of strong demand. In addition, our services may be subject to security or denial of services attacks which result in service interruptions or our customers may use our services in unanticipated ways that may cause a disruption in services for other customers. Since our customers use our service for important aspects of their business, any errors, defects, disruptions in service or other performance problems could result in negative publicity, damage to our reputation and brand, reduce our revenue, increase our operating expenses, negatively impact our ability to run our business, hinder our ability to enroll new customers, cause us to incur legal liability or issue refunds or service credits to our customers and cause us to lose current customers, all of which could substantially harm our business and operating results.

We utilize a hybrid cloud approach to our third-party data centers consisting of (i) two primary production data centers, located in Santa Clara, California, and Chicago, Illinois, which are each hosted by a third-party service provider and (ii) a network of Amazon Web Services (“AWS”) data centers which provides a distributed computing infrastructure platform for business operations. We maintain regular oversight but have little direct control over our two primary data centers. In the case of AWS, we do not control any aspects of the AWS data center operations and do not own any of the underlying computing hardware. We rely on these third-party service providers to provide continuous and uninterrupted access to our products and services, including Encompass and the Ellie Mae Network. If for any reason our relationship with any of these third parties were to end unexpectedly, it could require a significant amount of time to transition the hosting of our computing infrastructure to new third-party service providers.

We are also subject to interruptions beyond our and our third-party service providers’ control, such as disruptions or congestion in the portions of the Internet linking us to our customers. We are dependent on third parties for the

implementation and maintenance of certain aspects of our systems and because some of the causes of system interruptions may be outside of our control, we may not be able to remedy such interruptions in a timely manner. These interruptions may affect our customers' experience or cause us to lose customers, and may materially harm our reputation and operating results.



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Our failure to keep secure the confidential information of the customers of the users of our software and services could damage our reputation and brand and substantially harm our business and operating results.

We collect, process, transmit, and maintain certain confidential information relating to the customers (borrowers and loan applicants) of the users of our software and services, including personally identifiable information. This information resides on data center servers hosted by third-party providers, and is transmitted to, across, and from our networks. While we have security measures in place to protect this information and prevent security breaches, these security measures may be compromised as a result of third-party action, including intentional misconduct by computer hackers, advanced persistent cyber-attacks (by hacktivists or cybercriminal organizations), employee error or malfeasance, service provider or vendor error, malfeasance or other intentional or unintentional acts by third parties. Furthermore, our customers' data, including personally identifiable information, may be lost, exposed, or subject to unauthorized access and/or use as a result of accidents, errors, or malfeasance by our employees, independent contractors, or others working with us or on our behalf. Our servers and systems, and those of our service providers, may also be vulnerable to computer malware, break-ins, denial-of service attacks, and similar disruptions from unauthorized tampering with our computer systems, which could result in someone obtaining unauthorized access to our customers' data or our data, including our intellectual property and other confidential business information.

Because the techniques used to obtain unauthorized access to, or to sabotage, systems change frequently and often are not recognized until launched against a target, we may be unable to anticipate these techniques or implement adequate preventative measures. We may also experience security breaches that may remain undetected for an extended period. The possession and use of personally identifiable information in conducting our business subjects us to legislative and regulatory burdens that may require notification to customers in the event of a security breach, restrict our use of personally identifiable information, and hinder our ability to acquire new customers or market to existing customers. We cannot guarantee that our security measures will prevent security breaches or the loss or exposure of confidential information or other information we maintain or process. Any actual or perceived compromise of our security could result in the loss of customer data, intellectual property or trade secrets, and could damage our reputation and brand, negatively affect our ability to attract new customers and retain existing customers, adversely affect investor confidence, and expose us to a risk of litigation or regulatory actions and orders, penalties for violation of applicable laws, regulations, or contractual obligations and/or other liabilities, which would substantially harm our business and operating results. We will need to expend significant resources to protect against and remedy any potential security breaches and their consequences, including costs to deploy additional personnel and protection technologies, train employees, and engage third-party experts and consultants.

Our future performance will be highly dependent on our ability to continue to attract new Encompass customers and users of our other service offerings.

To maintain or increase our revenues, we may need to increase the number of users of our Encompass software and other service offerings, and the failure to do so may have a materially adverse impact on our business. If we are unable to increase the number of Encompass customers or users of our other services, our business may be materially adversely affected.

Our success will depend on (i) the willingness of mortgage lenders to continue to accept the SaaS model for delivering software applications that they view as critical to the success of their business, (ii) our ability to successfully deliver new and improved SaaS service offerings that meet the needs of mortgage lenders, (iii) the available market of potential users of our services and our ability to sell our services to these potential users.

It is difficult to predict customer adoption rates and demand for our services, the future growth rate and size of the market for our service offerings or the entry of competitive applications. The growth of the mortgage technology market depends on a number of factors, including the cost, performance, and perceived value associated with product offerings, most notably SaaS offerings such as our own, including the extent to which SaaS companies are successful in continuing to address security and reliability concerns. If other SaaS providers experience security incidents, loss of customer data, disruptions in delivery or other problems, the market for SaaS applications as a whole, including our own products and services, may be negatively affected. If there is a reduction in demand for mortgage technology caused by technological challenges, weakening economic conditions, interest rate increases, security or privacy concerns, competing technologies, and products, decreases in spending by mortgage lenders, a decrease in the number

of potential users of our service offerings, it could result in decreased revenues and our business could be adversely affected. In addition, we will need to continue to expand and optimize our sales infrastructure in order to grow our customer base and our business. Identifying and recruiting qualified personnel and training them in the use of our software requires significant time, expense, and attention.

If we are not able to provide successful enhancements, new features and modifications to our services, our business could be adversely affected. Further, impairment of software-related assets and other assets may materially adversely affect our operating results.

If we are unable to provide enhancements, new features, and modifications of our existing services, including the successful completion and deployment of our next generation Encompass software and the Encompass Lending Platform and changes to our services to reflect changes in laws and regulations relating to residential mortgage lending, our business and operating results could be adversely affected. In addition, if we do not successfully manage the migration of our customers to our next generation

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Encompass software or if the transition takes longer than expected, customers may not experience the benefits of new enhancements and features and our business and operating results could be adversely affected. In addition, we will need to continuously modify and enhance our services to keep pace with changes in software, communication, browser, database and SaaS infrastructure technologies. We may not be successful in either developing these modifications and enhancements or in bringing them to market in a timely fashion which could increase our costs and adversely affect our business. The failure of our services to operate effectively with future technologies could reduce the demand for our services, result in customer dissatisfaction and adversely affect our business.

We have invested and continue to invest significant resources to develop and acquire technology related to our services that is capitalized to property and equipment or intangible assets and treated as an asset on our balance sheet. We may not launch this new technology, the launch of such technology may result in disruptions to our business operations or such technology might not meet our and our customers' expectations. Also, changes to any of our implementation strategies or the failure of this technology to meet our and our customers' expectations could result in the impairment of software-related assets, and our future operating results could be materially adversely affected if we are required to write down the carrying value of capitalized software development or other intangible assets. A decrease in mortgage lending volume could materially adversely affect our business.

Mortgage lending volume decreased substantially in the first two quarters of 2017 relative to 2016 and may continue to decrease materially in the remaining quarters of 2017 and future years, which could materially adversely affect our business and our operating results. Factors that adversely impact mortgage lending volumes include increasing mortgage interest rates, reduced consumer and investor demand for mortgages, more stringent underwriting guidelines, decreased liquidity in the secondary mortgage market, high levels of unemployment, high levels of consumer debt, lower consumer confidence, changes in tax and other regulatory policies, the number of existing mortgages eligible for refinancing, the available inventory of housing and other macroeconomic factors.

Mortgage interest rates are influenced by a number of factors, including monetary policy. The Federal Reserve Bank raised the target federal funds rate by 0.25% in each of March 2017 and June 2017, the most recent increase from 1.00% to 1.25%, and signaled that the federal funds rate could be increased further over the next several years. The increase in the federal funds rate since December 2016 has contributed to an increase in mortgage interest rates in 2017 and may result in future mortgage interest rate increases. Increases in mortgage interest rates have materially reduced the volume of new mortgages originated in the first half of 2017 relative to 2016, in particular the volume of mortgage refinancings, and future increases may further decrease the volume of new mortgages originated. In addition, our on-demand revenues typically, but not always, track the seasonality of the residential mortgage industry, with increased activity in the second and third quarters and reduced activity in the first and fourth quarters as home buyers tend to purchase their homes during the spring and summer in order to move to a new home before the start of the school year. As a result, a higher percentage of our on-demand revenues have historically been recognized during those quarters.

We currently estimate that approximately 25% to 35% of our revenues have some direct sensitivity to volume. A decrease in residential mortgage volumes could materially adversely affect our business and operating results. Furthermore, a significant decrease in mortgage volume could negatively impact our customers, resulting in a reduction of their Encompass users, consolidation with other lenders or cessation of operations. If any of these occurs, it could materially adversely affect our business and operating results.

We cannot accurately predict subscription renewal or upgrade rates and the impact these rates may have on our future revenues and operating results.

Our customers have no obligation to renew their subscriptions for our service after the expiration of their initial subscription period, which ranges from one to five years. They may also choose to renew their subscriptions at lower levels. In addition, in the first year of a subscription, customers often purchase a higher level of professional services than they do in renewal years. As a result, our ability to grow is dependent in part on customers purchasing additional subscriptions and services after the initial subscription term. We cannot accurately predict renewal rates given our varied customer base and the number of multi-year subscription contracts. Our customers' renewal rates may decline or fluctuate because of several factors, including their satisfaction or dissatisfaction with our services, the prices of our services, changes to the standard prices of our services, the prices of services offered by our competitors or reductions

in our customers' spending levels due to the macroeconomic environment or other factors. If our customers do not renew their subscriptions for our services, renew on less favorable terms or do not purchase additional subscriptions or services, our revenues may grow more slowly than expected or decline and our profitability and gross margin percentage may be harmed.

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Our future performance will be highly dependent on our ability to expand the use of settlement services on, and increase the number of transactions effected through, the Ellie Mae Network.

To grow our base of Ellie Mae Network participants, we and settlement service providers must continue to enhance the features and functionality of offerings to them. In addition, increasing the number of settlement service transactions effected through the Ellie Mae Network will depend, in part, on settlement service providers enhancing their technical capabilities, which is largely beyond our control.

We must also convince a variety of potential Ellie Mae Network participants, including mortgage lenders, originators, settlement service providers, and mega lenders, of the benefits of electronic origination and network participation as compared to traditional mortgage origination methods including paper, facsimile, courier, mail, and email.

We cannot guarantee that our Ellie Mae Network and other service offerings will achieve market acceptance. In the event these efforts are not successful, our business and growth prospects would be adversely affected.

We expect a number of factors to cause our operating results to fluctuate on a quarterly and annual basis, which may make it difficult to predict our future performance.

Our revenues and operating results have in the past varied and could in the future vary significantly from quarter-to-quarter and year-to-year because of a variety of factors, many of which are outside of our control. As a result, comparing our operating results on a period-to-period basis may not be indicative of future operating results. In addition to other risk factors discussed in this section, factors that may contribute to the variability of our quarterly and annual results include:

- the number of Encompass users;
- the volume of mortgages originated by Encompass users, especially users on our Success-Based Pricing model;
- transaction volume on the Ellie Mae Network;
- fluctuations in mortgage lending volume and the number of closed loans relative to loan applications;
- the relative mix of purchase and refinance volume handled by Encompass users;
- the level of demand for our services;
- the timing of the introduction and acceptance of new services and Ellie Mae Network service providers;
- how quickly larger customers implement our services and use our services to originate and close loans;
- any write-downs in the value of our property and equipment, goodwill or intangible assets as a result of our investment or acquisition activities;
- costs associated with defending intellectual property infringement and other litigation claims;
- changes in accounting rules applicable to our business; and
- changes in government regulation affecting mortgage lenders and Ellie Mae Network participants or our business, and potential structural changes in the U.S. residential mortgage industry.

Due to these and other factors, our future results may not reach our financial projections. In addition, our operating results in future periods may not meet the expectations of investors or public market analysts who follow our company, which could cause our stock price to decline rapidly and significantly. The results of any prior quarterly or annual periods should not be relied upon as indications of our future operating performance.

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As we sell our services to larger customers, our sales cycle may become longer and more expensive, we may encounter pricing pressure and implementation challenges, and we may have to delay revenue recognition for some complex transactions or experience delays in these customers using our service to originate and close loans, all of which could harm our business and operating results.

Part of our business strategy is to target larger mortgage lenders that handle greater volumes of loans. As we target more of our sales efforts at larger customers, we could face greater costs, longer sales cycles, and less predictability in completing some of our sales. In this market, the customer's decision to use our products and services may be an enterprise-wide decision and, if so, this type of sale could require us to provide greater levels of education regarding the use and benefits of our products and services. In addition, larger customers may demand more complex integration, implementation services, and features, which may result in implementations that take longer than we forecast or plan or delays in these customers using our service to originate and close loans. As a result of these factors, these sales opportunities may require us to devote greater sales support and professional services resources to individual customers, driving up costs and time required to complete sales and diverting our own sales and professional services resources to a smaller number of larger transactions. Furthermore, if implementations take longer than planned or these customers delay their use of our service to originate and close loans, we may be required to delay revenue recognition on some of these transactions until the technical or implementation requirements have been met and may not generate on demand revenue from these customers as quickly as we had forecast.

If we are unable to scale our operations and increase productivity, we may not be able to successfully implement our business plan.

We continue to experience significant growth in our customer base, which has placed a strain on our management and administrative, operational, and financial infrastructure. Additional investments in our implementation capabilities, technical support, technical operations, research and development, and general and administrative functions will be required to scale our operations and increase productivity, address the needs of our customers, further develop and enhance our products and services, and scale with the overall growth of our company.

In addition, professional services, such as implementation services, are a key aspect of on-boarding new customers. The implementation process is complicated and we will need to scale our capabilities in this area to meet future revenue targets. If a customer is not satisfied with the quality of work performed by us or with the type of services or solutions delivered, then we could incur additional costs to address the situation, the profitability of that work might be impaired, and the customer's dissatisfaction with our products and services could damage our ability to obtain additional work from that customer. In addition, negative publicity related to our customer relationships, regardless of its accuracy, may further damage our business by affecting our ability to compete for new business with current and prospective customers.

Our growth strategy will require significant expenditures and resources to improve our technology, systems, and operational infrastructure in order to support a growing number of customers. We will need to make such expenditures with no assurance that the volume of our business or revenues will actually increase.

Our strategy of growing our business and increasing the number of Encompass users has placed and may continue to place significant demands on our technology systems and operational infrastructure. As our operations grow in size, scope, and complexity, we will need to expand, improve, and upgrade our technology systems and operational infrastructure, including the capabilities of the third-party data centers we utilize to offer an increasing number of customers enhanced solutions, features and functionality, and to ensure that our services are reliable.

Our growth and the improvement of our technology systems and operational infrastructure will require significant lead time and substantial financial, operational and technical resources in advance of the anticipated increase in the volume of business, with no assurance that the volume of business or our revenues will actually increase.

We have experienced rapid growth. If we fail to manage our growth effectively, we may be unable to execute our business plan, maintain high levels of service and operational controls or adequately address competitive challenges.

We have experienced, and are continuing to experience, a period of rapid growth in our customers, headcount, and operations. In particular, we grew from approximately 270 employees as of December 31, 2011 to 1,195 employees as of June 30, 2017, and have also significantly increased the number of customers and active users of Encompass. We anticipate that we will significantly expand our operations and headcount in the near term, and will continue to expand

our customer base. This growth has placed, and future growth will place, a significant strain on our management, general and administrative resources, and operational infrastructure.

Our success will depend in part on our ability to manage this growth effectively and to scale our operations. To manage the expected growth of our operations and personnel, we will need to continue to improve our operational, financial and management controls, and our reporting systems and procedures. As we continue to grow, we also need to ensure that our policies and procedures evolve to reflect our current operations and are appropriately communicated to and observed by employees, and that we

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appropriately manage our corporate information assets, including confidential and proprietary information. Failure to effectively manage growth could result in difficulty or delays in deploying customers, declines in quality or customer satisfaction, increases in costs, difficulties in introducing new features or other operational difficulties, and any of these difficulties could adversely impact our business performance and results of operations.

Completing and integrating future acquisitions could disrupt our business, harm our financial condition, and operating results or dilute or adversely affect the price of our common stock.

Our success will depend in part on our ability to expand our solutions and services and to grow our business in response to changing technologies, customer demands and competitive pressures. In some circumstances, we may pursue growth through the acquisition of complementary businesses, solutions or technologies rather than through internal development.

The identification of suitable acquisition candidates can be difficult, time-consuming, and costly, and we may not be able to complete acquisitions successfully. Moreover, if such acquisitions require us to seek additional debt or equity financing, we may not be able to obtain such financing on terms favorable to us or at all. Acquisitions and investments involve numerous risks which may have a negative impact on our results of operations, including:

- write-offs of acquired assets or investments;
- potential financial and credit risks associated with acquired customers;
- unknown liabilities associated with the acquired businesses;
- unanticipated expenses related to acquired technology and its integration into existing technology;
- limitations to our ability to recognize revenue from acquired deferred revenue;
- the potential loss of key employees;
- depreciation and amortization of amounts related to acquired intangible assets, fixed assets, and deferred compensation; and
- adverse tax consequences of any such acquisitions.

Even if we successfully complete an acquisition, we may not be able to assimilate and integrate effectively the acquired business, technologies, solutions, assets, personnel or operations, particularly if key personnel of an acquired company decide not to work for us. We may encounter difficulty in incorporating acquired technologies into our service and maintaining the quality standards that are consistent with our brand and reputation. In addition, we may issue debt or equity securities to complete an acquisition, which could dilute our stockholders' ownership and adversely affect the price of our common stock.

The residential mortgage industry is heavily regulated and changes in current legislation or new legislation could adversely affect our business.

The U.S. mortgage industry is heavily regulated. Federal and state governments and agencies could enact legislation or other policies that could negatively impact the business of our Encompass users and other Ellie Mae Network participants. In particular, the recent U.S. presidential transition may impact the substance and timing of legislation relating to the U.S. mortgage industry. Any changes to existing laws or regulations or adoption of new laws or regulations that increase restrictions on the residential mortgage industry may decrease residential mortgage volume or otherwise limit the ability of our Encompass users and Ellie Mae Network participants to operate their businesses, resulting in decreased usage of our solutions. In addition, reduced regulatory requirements may reduce the demand for certain of our products and services, including the Encompass Compliance service.

Changes in current legislation or new legislation may increase our costs by requiring us to update our products and services and if our products and services fail to address relevant mortgage lending laws and regulations our business could be adversely affected.

Changes to existing laws or regulations or adoption of new laws or regulations relating to the residential mortgage industry may require us to incur significant costs to update our products and services so that our customers remain compliant with such laws and regulations. Our Encompass Compliance Service analyzes mortgage loan data for compliance with consumer protection laws and institutionally mandated compliance policies and must continually be updated to incorporate changes to such laws and policies. The Dodd-Frank Act has caused and will continue to cause us to make similar updates to Encompass, Encompass Compliance Service, Encompass Product and Pricing Service, Encompass Docs Solution, TQL, and the Ellie Mae Network to address, among other things, regulations that protect



consumers against unfair, deceptive, and abusive practices by lenders. For example, additional tools and product updates were required to address the Ability-to-Repay/Qualified Mortgage and Federal and State High Cost rules that became effective in January 2014. In addition, we have updated certain products to comply with the TILA-RESPA Integrated Disclosure rule changes and the 2013 Loan Originator Rule under the Truth in Lending Act (Regulation Z) (TILA-RESPA Amendments) that became effective October 3, 2015. The final rule amending Regulation C to implement amendments to the Home Mortgage Disclosure Act (HMDA) made by section 1094 of the Dodd-Frank Act was published on

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October 15, 2015. It includes various effective compliance dates, starting with January 1, 2017 through May 30, 2020. The final "Qualified Residential Mortgage" rule which implements the risk retention requirements in the Dodd-Frank Act became effective on December 24, 2015. On August 23, 2016, Fannie Mae and Freddie Mac published the first material updates to the Uniform Residential Loan Application (URLA) in more than 20 years which will become effective in 2018. These additions and updates have caused us to incur significant expense, and future updates will likely cause us to incur similar significant expense. For example, if the new U.S. presidential administration and U.S. Congress significantly change or repeal the mortgage lending portions of the Dodd-Frank Act or the CFBP announces new rules or repeals previously announced rules, we may need to incur significant expense to make updates to our products and services. In addition, if our products and services fail to address relevant laws and regulations, we could be subject to claims by our customers that we have breached our customer contracts as well as potential claims by borrowers or government agencies. Such claims could result in substantial costs and we could incur judgments or enter into settlements of claims that could have a material adverse effect on our business and operating results. Furthermore, if our products and services fail to address relevant laws and regulations this could result in negative publicity, damage to our reputation and brand, hinder our ability to enroll new customers and cause us to lose current customers, all of which could substantially harm our business and operating results.

Potential structural changes in the U.S. residential mortgage industry, in particular plans to diminish the role of Fannie Mae and Freddie Mac, could disrupt the residential mortgage market and have a material adverse effect on our business.

Fannie Mae and Freddie Mac play a very important role in providing liquidity, stability, and affordability in the current U.S. residential mortgage market. In particular, they participate in the secondary mortgage market by purchasing mortgage loans and mortgage-related securities for investment and by issuing guaranteed mortgage-related securities. There have been numerous executive branch proposals as well as proposed federal legislation which may wind down or recapitalize Fannie Mae and Freddie Mac and/or eliminate or reduce the government's role in the housing market. Any significant structural change to the role of Fannie Mae and Freddie Mac or to the U.S. residential mortgage industry may cause significant disruption to the residential mortgage market. If we are unable to react effectively and quickly to changes in the residential mortgage industry or if such changes reduce the volume of mortgage lending, our business could be harmed.

We may be limited in the way in which we market our business or generate revenue by U.S. federal law prohibiting referral fees in real estate transactions, and if we are found to be in violation of such laws we would be subject to significant liability.

The Real Estate Settlement Procedures Act ("RESPA") generally prohibits the payment or receipt of fees or any other thing of value for the referral of business related to a residential real estate settlement service and prohibits fee shares or splits or unearned fees in connection with the provision of such services. Encompass software and services and the Ellie Mae Network were designed with payment methods that are intended to comply with the restrictions under RESPA. Nonetheless, RESPA may restrict our ability to enter into marketing and distribution arrangements with third parties for existing or newly developed products and services, particularly to the extent that such arrangements may be characterized as involving payments for the referral of residential real estate settlement service business. Additionally, any amendments to RESPA, court opinions interpreting the provisions of RESPA, or changes in the manner that RESPA is interpreted by the regulatory agencies responsible for enforcing RESPA, that result in restrictions on our current payment methods, or any determination that our payment methods have been and currently are subject to the restrictions under RESPA, could have a material adverse effect on our business. If we were found to be in violation of RESPA rules, we would be exposed to significant potential liability that could have a material adverse effect on our reputation and business.

We depend on key and highly skilled personnel to operate our business, and if we are unable to retain our current or hire additional personnel, our ability to develop and successfully market our business could be harmed.

We believe our future success will depend in large part upon our ability to attract and retain highly skilled managerial, technical, finance, creative, and sales and marketing personnel. Moreover, we believe that our future success is highly dependent on the contributions of our named executive officers. All of our officers and other employees are at-will employees, which means they may terminate their employment relationship with us at any time, and their knowledge

of our business and industry would be extremely difficult to replace. In addition, the loss of any key employees or the inability to attract or retain qualified personnel could delay the development and introduction of, and harm our ability to sell, our solutions and harm the market's perception of us. Competition for qualified personnel is particularly intense in the San Francisco Bay Area, where our headquarters are located. Qualified individuals are in high demand, and we may incur significant costs to attract them. We may be unable to attract and retain suitably qualified individuals who are capable of meeting our growing sales, operational and managerial requirements, or may be required to pay increased compensation in order to do so. If we are unable to attract and retain the qualified personnel we need to succeed, our business will suffer.

Volatility or lack of performance in our stock price may also affect our ability to attract and retain our key employees. Most of our named executive officers are vested in a substantial amount of stock options and Performance Awards. Employees may be more likely to leave us if the shares they own or the shares underlying their vested options have significantly appreciated in value relative to the original purchase prices of the shares or the exercise prices of the vested options, or if the exercise prices of the

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options that they hold are significantly above the market price of our common stock. If we are unable to retain our named executive officers or other key employees, our business will be harmed.

We operate in a highly competitive market, which could make it difficult for us to attract and retain Encompass users and Ellie Mae Network participants.

The mortgage origination software market is highly competitive. There are many software providers that compete with us by offering loan origination software to mortgage originators, such as: Byte Software Inc., a subsidiary of CBCInnovis; Calyx Technology, Inc.; DH Corporation; Lending QB, Mortgage Builder Software, Inc., a subsidiary of Altisource Portfolio Solutions SA; Mortgage Cadence, which is owned by Accenture PLC; Wipro Gallagher Solutions, which is owned by Wipro, Ltd.; and LoanSphere Empower and LoanSphere LendingSpace, which are owned by Black Knight Financial Services, Inc. Some software providers, including Calyx Technology, Inc. and Black Knight Financial Services, Inc., also provide connectivity between their software users and lenders and service providers to make such services available to mortgage lenders. We also compete with compliance, document preparation service, and product eligibility and pricing service providers that are more established than us. There is vigorous competition among providers of these services and we may not succeed in convincing potential customers using other services to switch to ours. In addition, some of our competitors are consolidating which facilitates greater cross-selling of services, which could weaken our ability to differentiate our offering in the market. Some of our competitors also offer services on a per closed loan basis, which could adversely impact the effectiveness of our Success-Based Pricing strategy for increasing the number of Encompass customers. If we are unsuccessful in competing effectively by providing attractive functionality, customer service or value, we could lose existing Encompass users to our competitors and our ability to attract new Encompass users could be harmed.

There are many service providers that offer our Encompass users competing services, including borrower-facing websites, customer relationship management solutions, document preparation services, compliance services, product eligibility and pricing services, and electronic document management services. We may be unsuccessful in continuing to differentiate our Encompass service offerings to the extent necessary to effectively compete in some or all of these markets.

The Ellie Mae Network is only available to mortgage originators using Encompass. The principal alternative to the use of the Ellie Mae Network by Encompass users remains traditional methods of exchanging data and documents among mortgage industry participants by email, facsimile, phone, courier, and mail. In addition, mortgage originators may use standalone web browsers to go individually to each investor, lender or service provider's website, and then manually upload loan data or enter information into the website. Mortgage originators may continue to use these methods due to habit, personal business relationships or otherwise. The success of the Ellie Mae Network depends on our ability to achieve and offer access to both the critical mass of investors, lenders, and service providers necessary to attract and retain mortgage originators using Encompass on the Ellie Mae Network and the critical mass of active mortgage originators necessary to attract and retain investors, lenders, and service providers on our network.

Some of our actual and potential competitors have longer operating histories and significantly greater financial, technical, marketing, and other resources than we do and, as a result, these companies may be able to respond more quickly to changes in regulations, new technologies or customer demands, or devote greater resources to the development, promotion, and sale of their software and services than we can. In addition, we may face increased competition as a result of continuing industry consolidation. We expect the mortgage origination market to continue to attract new competitors and there can be no assurance that we will be able to compete successfully against current or future competitors or that competitive pressures we face will not materially adversely affect our business.

Failure to adapt to technological changes may render our technology obsolete or decrease the attractiveness of our solutions to our customers.

If new industry standards and practices emerge, or if competitors introduce new solutions embodying new services or technologies, Encompass and the Ellie Mae Network technology may become obsolete. Our future success will depend on our ability to:

- enhance our existing solutions;
- develop and potentially license new solutions and technologies that address the needs of our prospective customers;
- and

respond to changes in industry standards and practices on a cost-effective and timely basis.

We must continue to enhance the features and functionality of Encompass, our other services, and the Ellie Mae Network. The effective performance, reliability, and availability of Encompass, our other services, and the Ellie Mae Network infrastructure are critical to our reputation and our ability to attract and retain Encompass users, users of our other services and Ellie Mae Network participants. If we do not continue to make investments in product development and, as a result, or due to other reasons, fail to attract new and retain existing mortgage originators, lenders, investors, and service providers, we may lose existing Ellie Mae

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Network participants, which could significantly decrease the value of the Ellie Mae Network to all participants and materially adversely affect our business.

We are subject to the risks of current and future legal proceedings, which could have a material adverse effect on our business, financial condition, results of operations, and future prospects.

At any given time, we are a defendant in various legal proceedings and litigation matters arising in the ordinary course of business including commercial and employment disputes. We can give no assurance that the outcome of any such matter would not have a material adverse effect on our consolidated financial condition, results of operations or cash flows. We are unable to predict the ultimate outcome of these disputes or the actual impact of these matters on our profitability at this time, and any views we form as to the viability of these claims or the financial exposure in which they could result, could change from time to time as the matters proceed through their course, as facts are established, and various judicial determinations are made.

If we agree to settle these matters or judgments are secured against us, we may incur charges which may have a material and adverse impact on our business, financial conditions, results of operations, and future prospects.

Failure to adequately protect our intellectual property could harm our business.

The protection of our intellectual property rights, including our proprietary Encompass software and Ellie Mae Network technology, is crucial to the success of our business. We rely on a combination of patent, copyright, trademark and trade secret law, and contractual restrictions to protect our intellectual property. Our present and future patents may provide only limited protection for our technology and may not be sufficient to provide competitive advantage to us. Furthermore, we cannot guarantee any patents will be issued to us as a result of our patent applications. We also rely in part on confidentiality and invention assignment agreements with our employees, independent contractors, and consultants. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our Ellie Mae Network and Encompass features and functionality or obtain and use information that we consider proprietary. Enforcing our proprietary rights is difficult and may not always be effective. We have registered “Ellie Mae,” “Encompass,” and “AllRegs” and certain of our other trademarks as trademarks in the United States. Competitors may adopt service names similar to ours, thereby impeding our ability to build brand identity and possibly leading to customer confusion. In addition, there could be potential trade name or trademark infringement claims brought by owners of other registered trademarks or trademarks that incorporate variations of the terms Ellie Mae, Encompass or our other trademarks.

Litigation or proceedings before the U.S. Patent and Trademark Office or other governmental authorities and administrative bodies in the United States and abroad may be necessary in the future to enforce our intellectual property rights, protect our patent and copyright rights, trade secrets and domain names, and determine the validity and scope of the proprietary rights of others. Our efforts to enforce or protect our proprietary rights may be ineffective and could result in substantial costs and diversion of resources and could harm our business.

Assertions that we infringe third-party intellectual property rights could result in significant costs and substantially harm our business.

Other parties have asserted, and may in the future assert, that we have infringed their intellectual property rights. In addition, we generally agree to indemnify our customers against legal claims that our software products infringe intellectual property rights of third parties and, in the event of an infringement, to modify or replace the infringing product or, if those options are not reasonably possible, to refund the cost of the software, as pro-rated over a period of years. We cannot predict whether assertions of third-party intellectual property rights or claims arising from such assertions will substantially harm our business and operating results. If we are forced to defend against any infringement claims, whether they are with or without merit or are determined in our favor, we may face costly litigation and diversion of technical and management personnel. Furthermore, an adverse outcome of a dispute may require us to: pay damages, potentially including treble damages and attorneys’ fees if the infringement were found to be willful; cease providing solutions that allegedly incorporate the intellectual property of others; expend additional development resources to redesign or re-engineer our solutions and products, if feasible; and enter into potentially unfavorable royalty or license agreements in order to obtain the right to use necessary technologies. We cannot be certain of the outcome of any litigation. Any royalty or licensing agreement, if required, may not be available to us on acceptable terms or at all. Our failure to obtain the necessary licenses or other rights could prevent the sale or

distribution of some of our products and services and, therefore, could have a material adverse effect on our business. Our internal information technology systems are critical to our business. System integration and implementation issues could disrupt our operations, which could have a material adverse impact on our business or results in significant deficiencies or material weaknesses in our internal controls.

We rely on the efficient and uninterrupted operation of complex information technology systems, including systems for customer billing, human resources, enterprise resource planning and customer relationship management. As our business has grown in size and complexity, the growth has placed, and will continue to place, significant demands on our internal information

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technology systems. To effectively manage this growth, we must commit significant financial resources and personnel to maintain and enhance existing systems and develop or acquire new systems to keep pace with continuing changes in our business and information processing technology as well as evolving industry, regulatory and accounting standards. If the information we rely upon to run our businesses is determined to be inaccurate or unreliable, if we fail to properly maintain or enhance our internal information technology systems, we could have operational disruptions, customer disputes, significant deficiencies or material weaknesses in our internal controls, have increases in operating and administrative expenses, lose our ability to produce timely and accurate financial reports, or suffer other adverse consequences.

If we fail to maintain proper and effective internal controls, our ability to produce accurate financial statements could be impaired, which could result in a loss of investor confidence in our financial reports, significant expenses to remediate any internal control deficiencies, and ultimately have an adverse effect on the market price of our common stock.

As a publicly-traded company, we are subject to compliance with, among other regulations, Section 404 of the Sarbanes-Oxley Act of 2002, or SOX, which requires that we test our internal control over financial reporting and disclosure controls and procedures. Ensuring that we have adequate internal financial and accounting controls and procedures in place so that we can produce accurate financial statements on a timely basis is a costly and time-consuming effort that needs to be re-evaluated frequently. Our compliance with SOX requires that we incur substantial expense and expend significant management time on compliance-related issues. If we fail to achieve and maintain an effective internal control environment, we could suffer material misstatements in our financial statements and fail to meet our reporting obligations, which would likely cause investors to lose confidence in our reported financial information. This could harm our operating results and lead to a decline in our stock price. Additionally, ineffective internal control over financial reporting could expose us to increased risk of fraud or misuse of corporate assets and subject us to potential delisting from the New York Stock Exchange, regulatory investigations, civil or criminal sanctions, and class action litigation.

As a third-party technology service provider of mission-critical products and services to many financial institutions that are regulated by one or more member agencies of the Federal Financial Institutions Examination Council, or FFIEC, we are subject to an IT examination by the member agencies of the FFIEC. As a result, the FFIEC conducts recurring IT Examinations in order to identify existing or potential risks associated with our operations that could adversely affect the financial institutions to whom we provide products and services, evaluate our risk management systems, and controls and determine our compliance with applicable laws that affect the products and services we provide to financial institutions. In addition to examining areas such as our management of technology, data integrity, information confidentiality, and service availability, the reviews also assess our financial stability. In June 2014, the FDIC, a member agency of the FFIEC, completed its IT examination, and found that, while the services we provide to our client banks are satisfactory, several matters required further attention, some of which were repeat findings and recommendations from the FDIC's 2012 examination. Although management has developed a plan for addressing these matters, we cannot be assured that the plan will satisfy the FDIC or applicable law. A sufficiently unfavorable review from the FFIEC in the future could have a material adverse effect on our business and financial condition. If one or more U.S. states or local jurisdictions successfully assert that we should have collected or in the future should collect additional sales or use taxes on our fees, we could be subject to additional liability with respect to past or future sales, and the results of our operations could be adversely affected.

We do not collect state and local sales and use taxes on all sales in all jurisdictions in which our customers are located, based on our belief that such taxes are not applicable. Sales and use tax laws and rates vary by jurisdiction and such laws are subject to interpretation. Jurisdictions in which we do not collect sales and use taxes may assert that such taxes are applicable, which could result in the assessment of such taxes, interest, and penalties, and we could be required to collect such taxes in the future. This additional sales and use tax liability could adversely affect the results of our operations.

Our business is subject to the risks of earthquakes, fires, floods, and other natural catastrophic events and to interruption by man-made problems such as terrorism.



Our systems and operations are vulnerable to damage or interruption from earthquakes, fires, floods, power losses, telecommunications failures, terrorist attacks, acts of war, and similar events. For example, a significant natural disaster, such as an earthquake, fire or flood, could have a material adverse impact on our business, operating results and financial condition, and our insurance coverage may be insufficient to compensate us for losses that may occur. Our corporate offices and one of the facilities we lease to house our computer and telecommunications equipment are located in the San Francisco Bay Area, a region known for seismic activity. In addition, acts of terrorism, which may be targeted at metropolitan areas with higher population density than rural areas, could cause disruptions in our or our customers' businesses or the economy as a whole. We may not have sufficient protection or recovery plans in certain circumstances, such as natural disasters affecting the San Francisco Bay Area, and our business interruption insurance may be insufficient to compensate us for losses that may occur.

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Our stock price is volatile and purchasers of our common stock could incur substantial losses.

The trading price of our common stock may be subject to wide fluctuations in response to various factors, some of which are beyond our control. In addition to the factors discussed in this “Risk Factors” section and elsewhere in our filings with the SEC, these factors include:

- our operating performance and the operating performance of similar companies;
- the overall performance of the equity markets;
- the number of shares our common stock publicly owned and available for trading;
- threatened or actual litigation;
- changes in laws or regulations relating to our solutions;
- any major change in our board of directors or management;
- publication of research reports about us or our industry or positive or negative recommendations or withdrawal of research coverage by securities analysts;
- large volumes of sales of our shares of common stock by existing stockholders; and
- general political and economic conditions.

In addition, the stock market in general has experienced extreme price and volume fluctuations. Securities class action litigation has often been instituted against companies following periods of volatility in the overall market and in the market price of a company’s securities. This litigation, if instituted against us, could result in very substantial costs, divert our management’s attention and resources and harm our business.

Our reported financial results may be adversely affected by changes in accounting principles generally accepted in the United States.

Generally accepted accounting principles in the United States are subject to interpretation by the Financial Accounting Standards Board (FASB), the SEC, and various bodies formed to promulgate and interpret appropriate accounting principles. A change in these principles or interpretations could have a significant effect on our reported financial results, and could affect the reporting of transactions completed before the announcement of a change. For example, the adoption of ASC 606, a new revenue recognition standard, which becomes effective in fiscal 2018, could impact the timing of recognition of certain revenue streams, as well as how we account for certain commissions. Further, the evaluation and implementation of new standards, including ASC 606, may require additional resources and system configurations that could increase our operating costs.

We may execute stock repurchase programs, when authorized by the board of directors, that may be suspended or terminated at any time, which may result in a decrease in the trading price of our common stock.

Such stock repurchases may be limited, suspended, or terminated at any time without prior notice. There can be no assurance that we will repurchase additional shares of our common stock under our stock repurchase program or that any future repurchases will have a positive impact on the trading price of our common stock or earnings per share. Important factors that could cause us to limit, suspend or terminate our stock repurchase program include, among others, unfavorable market conditions, the trading price of our common stock, the nature of other investment or strategic opportunities presented to us from time to time, the rate of dilution of our equity compensation programs, the availability of adequate funds, and our ability to make appropriate, timely, and beneficial decisions as to when, how, and whether to purchase shares under the stock repurchase program. If we limit, suspend or terminate our stock repurchase program, our stock price may be negatively affected.

If securities or industry analysts discontinue publishing research or publish inaccurate or unfavorable research about our business, our stock price could decline.

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

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Certain provisions in our charter documents and Delaware law could discourage takeover attempts and lead to management entrenchment.

Our amended and restated certificate of incorporation and amended and restated bylaws contain provisions that could have the effect of delaying or preventing changes in control or changes in our board of directors. These provisions include:

- a classified board of directors with three-year staggered terms, which may delay the ability of stockholders to change the membership of a majority of our board of directors;
- no cumulative voting in the election of directors, which limits the ability of minority stockholders to elect director candidates;
- the exclusive right of our board of directors to elect a director to fill a vacancy created by the expansion of the board of directors or the resignation, death or removal of a director, which prevents stockholders from being able to fill vacancies on our board of directors;
- the ability of our board of directors to determine to issue shares of preferred stock and to determine the price and other terms of those shares, including preferences and voting rights, without stockholder approval, which could be used to significantly dilute the ownership of a hostile acquirer;
- a prohibition on stockholder action by written consent, which forces stockholder action to be taken at an annual or special meeting of our stockholders;
- the requirement that a special meeting of stockholders may be called only by the chairman of the board of directors, the chief executive officer, the president or the board of directors, which may delay the ability of our stockholders to force consideration of a proposal or to take action, including the removal of directors; and
- advance notice procedures that stockholders must comply with in order to nominate candidates to our board of directors or to propose matters to be acted upon at a stockholders' meeting, which may discourage or deter a potential acquirer from conducting a solicitation of proxies to elect the acquirer's own slate of directors or otherwise attempting to obtain control of us.

We are also subject to certain anti-takeover provisions under Delaware law. Under Delaware law, a corporation may not, in general, engage in a business combination with any holder of 15% or more of its capital stock unless the holder has held the stock for three years or, among other things, the board of directors has approved the transaction.

**ITEM 2—UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The table below sets forth the information with respect to purchases made by or on behalf of the Company or any "affiliated purchaser" (as the term is defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934, as amended) of our common stock during the three months ended June 30, 2017:

**ISSUER PURCHASES OF EQUITY SECURITIES**

| Period                          | Total<br>Number<br>of<br>Shares<br>Purchased | Average<br>Price<br>Paid<br>per<br>Share | Total<br>Number<br>of Shares<br>Purchased<br>as<br>Part of<br>Publicly<br>Announced<br>or<br>Programs | Approximate<br>Dollar Value<br>or<br>Shares that<br>May<br>Yet be<br>Purchased<br>Under the<br>Plans<br>or Programs<br>(1) |
|---------------------------------|----------------------------------------------|------------------------------------------|-------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------|
|                                 |                                              |                                          |                                                                                                       |                                                                                                                            |
| April 1, 2017 to April 30, 2017 | —                                            | \$                                       | —                                                                                                     | \$ 42,806,483<br>(1)                                                                                                       |
| May 1, 2017 to May 31, 2017     | —                                            | \$                                       | —                                                                                                     | \$ 42,806,483<br>(1)                                                                                                       |
| June 1, 2017 to June 30, 2017   | —                                            | \$                                       | —                                                                                                     | \$ —                                                                                                                       |

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<sup>(1)</sup> In May 2014, our board of directors approved a stock repurchase program under which we are authorized to repurchase up to \$75.0 million of our common stock in which all shares are retired upon repurchase. This program ended in May 2017.

ITEM 3—DEFAULTS UPON SENIOR SECURITIES

Not applicable.

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ITEM 4—MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5—OTHER INFORMATION

Not applicable.

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ITEM 6—EXHIBITS

| Exhibit Number | Description of Document                                                                                                                                                          |
|----------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1           | Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2           | Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1*          | Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.                               |
| 32.2*          | Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.                               |
| 101.INS        | XBRL Instance Document                                                                                                                                                           |
| 101.SCH        | XBRL Taxonomy Extension Schema Document                                                                                                                                          |
| 101.CAL        | XBRL Taxonomy Extension Calculation Linkbase Document                                                                                                                            |
| 101.DEF        | XBRL Taxonomy Extension Definition Linkbase Document                                                                                                                             |
| 101.LAB        | XBRL Taxonomy Extension Label Linkbase Document                                                                                                                                  |
| 101.PRE        | XBRL Taxonomy Extension Presentation Linkbase Document                                                                                                                           |

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Exhibits 32.1 and 32.2 are being furnished and shall not be deemed to be “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, nor shall such exhibits be deemed to be incorporated by reference in any registration statement or other document filed under the Securities Act of 1933, as amended, or the Exchange Act, except as otherwise specifically stated in such filing.

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SIGNATURES

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

ELLIE MAE, INC.

Date: August 3, 2017 By: /s/ Matthew LaVay

Matthew LaVay

Executive Vice President and

Chief Financial Officer

(Principal Financial and Accounting Officer and duly authorized signatory)