Paycom Software, Inc.
Form 10-K
February 14, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2018

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission file number: 001-36393

Paycom Software, Inc.

(Exact name of registrant as specified in its charter)

Delaware	80-0957485
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

7501 W. Memorial Road

Oklahoma City, Oklahoma 73142

(Address of registrant's principal executive offices)

Registrant's telephone number, including area code: (405) 722-6900

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $0.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 every Interactive Data File required to be submitted 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 such files). Yes No

Indicate by a check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the

Exchange Act.

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

As of February 5, 2019, 58,599,531 shares of the registrant's common stock, $0.01 par value per share, were outstanding, including 1,322,539 shares of restricted stock. As of June 30, 2018, the aggregate market value of voting stock held by non-affiliates of the registrant was approximately $4.9 billion (based on the closing price for shares of the registrant's common stock as reported by the New York Stock Exchange on June 29, 2018, the last trading day of the registrant's most recently completed second fiscal quarter).

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Definitive Proxy Statement on Schedule 14A to be furnished to stockholders in connection with its 2019 Annual Meeting of Stockholders are incorporated by reference in Part III, Items 10-14 of this Annual Report on Form 10-K.

PAYCOM SOFTWARE, INC.

2018 ANNUAL REPORT ON FORM 10-K

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PART I

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K (this "Form 10-K") contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements are any statements that look to future events and include, but are not limited to, statements regarding our business strategy; anticipated future operating results and operating expenses, cash flows, capital resources, dividends and liquidity; trends, opportunities and risks affecting our business, industry and financial results; future expansion or growth plans and potential for future growth; our ability to attract new clients to purchase our solution; our ability to retain clients and induce them to purchase additional applications; our ability to accurately forecast future revenues and appropriately plan our expenses; market acceptance of our solution and applications; our expectations regarding future revenues generated by certain applications; our ability to attract and retain qualified employees and key personnel; future regulatory, judicial and legislative changes; how certain factors affecting our performance correlate to improvement or deterioration in the labor market; our plan to open additional sales offices and our ability to effectively execute such plan; the sufficiency of our existing cash and cash equivalents to meet our working capital and capital expenditure needs over the next 12 months; our ability to relocate our Texas operations facility within an expected timeframe; our plans regarding our capital expenditures and investment activity as our business grows, including with respect to our new Texas operations facility and research and development; the expected impact on our consolidated financial statements of new accounting pronouncements; our plans to repurchase shares of our common stock through a stock repurchase plan; and our expected income tax rate for future periods. In addition, forward-looking statements also consist of statements involving trend analyses and statements including such words as "anticipate," "believe," "could," "expect," "will," "intend," "may," "might," "plan," "potential," "should," "would," and similar expressions or the negative of such terms or othe comparable terminology. These forward-looking statements speak only as of the date of this Form 10-K and are subject to business and economic risks. As such, our actual results could differ materially from those set forth in the forward-looking statements as a result of the factors set forth below in Part I, Item 1A, "Risk Factors," and in our other reports filed with the Securities and Exchange Commission (the "SEC"). We do not undertake any obligation to update or revise the forward-looking statements to reflect events that occur or circumstances that exist after the date on which such statements were made, except to the extent required by law.

Item 1. Business

Unless we state otherwise or the context otherwise requires, the terms "Paycom," "we," "us," "our" and the "Company" refer t Paycom Software, Inc., a Delaware corporation, and its consolidated subsidiaries.

Overview

We are a leading provider of comprehensive, cloud-based human capital management ("HCM") solution delivered as Software-as-a-Service ("SaaS"). We provide functionality and data analytics that businesses need to manage the complete employment lifecycle, from recruitment to retirement. Our solution requires virtually no customization and is based on a core system of record maintained in a single database for all HCM functions, including talent acquisition, time and labor management, payroll, talent management and human resources ("HR") management applications. Our user-friendly software allows for easy adoption of our solution by employees, enabling self-management of their HCM activities in the cloud, which reduces the administrative burden on employers and increases employee productivity.

Organizations need sophisticated, flexible and intuitive applications that can quickly adapt to their evolving HCM requirements, streamline their HR processes and systems and enable them to control costs. We believe the HCM needs of most organizations are currently served either by multiple providers in an attempt to replicate a comprehensive SaaS product or, to a lesser extent, by legacy providers offering outdated on-premise products. These approaches often result in challenges with system integration and data integrity, low scalability, high costs, extended delivery times and large up-front capital requirements.

Because our solution was developed in-house and is based on a single platform, there is no need to integrate, update or access multiple databases, which are common issues with competitor offerings that use multiple third-party systems in order to link together their HCM offerings. Additionally, our solution maintains data integrity for accurate, actionable and real-time analytics and business intelligence and helps clients minimize the risks of compliance errors due to inaccurate or missing information. We deliver feature-rich applications while maintaining excellence in information security and quality management standards, as evidenced by our International Organization for Standardization (“ISO”) certifications.

We sell our solution directly through our internally trained, client-focused and highly skilled sales force based in offices across the United States. As a part of our client retention effort, a specialist within a dedicated team is assigned to each client to provide industry-leading, personalized service. We have over 23,500 clients, none of which constituted more than one-half of one percent of our revenues for the year ended December 31, 2018. We believe that as a result of our focus on client retention, we enjoy high client satisfaction as evidenced by an annual revenue retention rate of 92%, 91% and 91% from existing clients for the years ended December 31, 2018, 2017 and 2016, respectively. We believe our revenue retention rate understates our client loyalty because this rate is decreased by former clients that were acquired or otherwise ceased operations.

We were founded in 1998. Since our founding, we have focused on providing an innovative SaaS HCM solution. As of December 31, 2018, we had 3,050 employees across the United States. For the years ended December 31, 2018, 2017 and 2016, our revenues were $566.3 million, $433.0 million and $329.1 million, respectively, representing year-over-year growth in revenues of approximately 31% and 32%, respectively. We currently derive the majority of our revenues from payroll processing. We are able to determine revenues from payroll processing because all of our clients are required to utilize our payroll application in order to access our other applications. We generally do not separately track our revenues across our other applications because we often sell applications in various groupings and configurations for a single price. We realized net income of $137.1 million, $123.5 million and $70.4 million for the years ended December 31, 2018, 2017 and 2016, respectively.

The Paycom Solution

We offer an end-to-end SaaS HCM solution that provides our clients and their employees with immediate access to accurate and secure information and analytics at any time from any location where internet service is available. We believe our solution delivers the following benefits:

Comprehensive HCM Solution

Our solution offers functionality that manages the entire employment lifecycle for employers and employees, from recruitment to retirement. Our user-friendly applications streamline client processes and provide clients and their employees with the ability to directly access and manage administrative processes, including applications that identify candidates, on-board employees, manage time and labor, administer payroll deductions and benefits, manage performance, terminate employees and administer post-termination health benefits such as COBRA. The widespread employee usage of our applications further integrates our solution into the administrative processes of our clients. Our solution also has the advantage of being built in-house by our highly trained and skilled team of software developers, thereby minimizing data integrity issues across applications.

Core System of Record

Our solution is based on a core system of record that contains payroll and HR information in one convenient database, thereby reducing costs and eliminating the need for multiple software products and vendors and the maintenance of employee data in numerous databases. This core system of record enables our clients to input employee data one time and enjoy seamless functionality across our applications. When a revision is made to the file of an employee, all appropriate personnel have access to the change in real time. In addition, our core system of record helps clients minimize the risk of compliance errors due to inaccurate or missing information that results from maintaining multiple databases. Through accurate tracking and management of employee payroll and other HR data, such information can be compiled for comprehensive and consistent reporting for our clients.

Data Analytics and Business Intelligence

Our solution’s core system of record allows clients to strategically analyze comprehensive and accurate employee information to make informed business decisions based upon actionable, real-time analytics provided through our client dashboard. This functionality allows our clients to operate with a more complete and accurate picture of their organization, as our solution’s embedded analytics capture the content and context of everyday business events, facilitating fast and informed decision-making from any location. These tools help clients reduce administrative and operational costs and better manage talent.

Enhanced Employee Experience

The employees of our clients also benefit from our HCM applications. As workforces transition from technology-savvy to technology-dependent, employees expect mobile technology and the resources necessary to readily access information and control their professional development. Through our employee self-service technology, employees can view real-time HR information, including pay stubs, W-2s and benefits information, as well as manage their schedules and vacation time and update W-4 contact information. Our mobile apps, available on both the Google Play™ store and the App Store® online store, make it easier for employees to access their self-service information. Our apps have fingerprint and facial recognition capabilities, aiding employers in their efforts to engage technology-dependent workers. Our system also allows employers to engage their workforce through learning management courses and training paths, surveys, and performance goals and reviews.

In addition to our self-service, app-based functionality, we also provide our clients with a strategy to drive usage among their employees. This strategy includes training clients' employees how to use the Paycom app during implementation and providing additional training from our client relations representatives. Allowing employees to make changes directly to our database creates efficiencies for both the employer and employee. Today's employees have little tolerance for complexity, and with our solution, employees have become accustomed to having a direct relationship with their HR database. This relationship is directly correlated with our single-database that is key to increasing usage. Our strategy to promote employee usage of the Paycom system elevates HR personnel to focus on the human element of their jobs, creating a more positive culture and giving HR personnel more time to engage with their employees.

Personalized Support Provided by Trained Personnel

Our applications are supported by one-on-one personal assistance from trained specialists. Service specialists are assigned to specific clients and are trained across all of our applications, ensuring they provide comprehensive, expert-level service. Our client service is ISO 9001:2015 certified on the basis of its quality and consistency. We strive to provide our clients with high levels of service and support to ensure their continued use of our solution for all of their HCM needs. We have maintained high client satisfaction, as evidenced by an annual revenue retention rate of 92%, 91% and 91% from existing clients for the years ended December 31, 2018, 2017 and 2016, respectively.

Software-as-a-Service Delivery Model

Our SaaS delivery model allows clients with geographically dispersed and mobile workforces to operate more efficiently, and allows these clients to implement, access and use our client-oriented internet solution on demand and remotely through standard web browsers, smart phones, tablets and other web-enabled devices. Our SaaS solution reduces the time, risk, headcount and costs associated with installing and maintaining applications for on-premise products within the information technology (“IT”) infrastructure of our clients.

Secure Cloud-Based Architecture

Our cloud-based architecture allows our solution to be implemented remotely with minimal client interaction. Updates such as software enhancements and newly developed applications can be deployed without client interaction, disruption or involvement, allowing our clients to make a smaller investment in hardware, personnel, implementation time and consulting. Additionally, we own and maintain all of the infrastructure technology to host our solution and to maximize system availability for clients. Our focus on, and investment in, technology and data security has been recognized with ISO/IEC 27001:2013 certified security standards that provide our clients with a “best-in-class” level of data security.

Scalability to Grow with our Clients

Our solution is highly scalable. We serve a diversified client base ranging in size from one employee to many thousands of employees, while our target client size range is 50 to 5,000 employees. We calculate the number of clients’ employees based on parent company grouping. Our clients are able to use the same solution while their businesses grow by deploying applications as-needed in real-time. Pricing is determined by employee headcount and the number of applications utilized, enabling our clients to align HCM spending with their evolving HCM needs as compared to traditional HCM products that require clients to migrate to new software as they grow but retain fixed costs even if the client shrinks in size.

Efficient and Productive Research and Development

We believe we benefit from a competitive advantage with our research and development investments, people and processes. Early investments in our proprietary, cloud-based architecture enable us to develop and deploy applications in a timely and cost-effective manner. We have also chosen to base our research and development team in Oklahoma and Texas, which we believe provides us with high-quality talent at a lower cost compared to other locations in the United States where there is more competition for technology talent. These strategic decisions have enabled us to have a highly productive research and development function.

Our Strategy for Growth

Our strategy is to continue to establish our solution as the HCM industry standard by increasing our presence in existing markets and expanding into additional markets. We intend to continue to open new sales offices as well as potentially expand over the longer term into international markets. We will also execute our strategy for growth by targeting larger clients, as well as strengthening and extending our solution.

Increase Our Presence in Existing Markets

We believe a significant market opportunity exists to increase our presence within markets where we currently have a sales office. Each sales office is typically staffed with one sales team, with each team comprised of a sales manager and approximately six to eight other sales professionals. Although we have a sales office in 37 of the 50 largest metropolitan statistical areas ("MSAs") in the United States based on July 2017 U.S. Census Bureau estimates, only five of these MSAs are currently served by multiple Paycom sales teams. In addition to expanding into new markets, we plan to further penetrate and more effectively capture existing markets by adding sales offices and increasing the number of sales teams in such markets. Since our initial public offering ("IPO") in April 2014, we have expanded our presence within three MSAs that were already served by at least one Paycom sales team by opening new sales offices in Brooklyn, Chicago, Long Island and Pasadena.

Expand Into Additional Markets

We plan to continue expanding our sales capability by opening sales offices in certain metropolitan areas where we currently have no sales teams. Since our IPO in April 2014, we have expanded into 14 new markets.

We have historically selected new locations based on potential client and employee demographics as well as business density. When opening a new sales office, we typically relocate a proven sales manager from an existing territory who then recruits a team of high-performing sales representatives. It typically takes a new sales office 24 months to reach maturity.

Enlarge our Existing Client Relationships

We dedicate our resources to helping our clients facilitate their goals, whether through helping them execute better hiring decisions, manage compensation more effectively or simply operate more efficiently. We believe a significant growth opportunity exists in selling additional applications to our current clients. Many clients have subsequently deployed additional applications as they recognize the benefits of our comprehensive solution. As we extend and enhance the functionality of our solution, we will continue to invest in initiatives to increase the adoption of our solution and maintain our high levels of client satisfaction.

Target Larger Clients

The average size of our clients has grown significantly as we have organically grown our operations and increased the number of applications we offer. We serve a diversified client base ranging in size from one employee to many thousands of employees, while our target client size is 50 to 5,000 employees. Based on our total revenues, we have grown at a 39% compound annual growth rate from January 1, 2015 through December 31, 2018. Our solution requires no adjustment to serve larger clients. We believe larger employers represent a substantial opportunity to increase the number of clients and to increase our revenues per client, with limited incremental cost to us. To further capitalize on this opportunity, we intend to continue targeting larger businesses opportunistically where our current sales model is effective.

Maintain Our Leadership in Innovation by Strengthening and Extending our Solution

Our ability to develop and deploy new applications and updates rapidly and cost-effectively has been integral to the results that we have achieved to date. We intend to continue extending the functionality and range of our solution in the future. Our development efforts are performed exclusively in-house and are heavily based upon proactive research and client input. We are focusing our investments on the development of new applications, enhancements and learning courses that are responsive to the needs of our clients, which are garnered through ongoing client interaction and collaboration.

Our Applications

Our HCM solution offers a full suite of applications that generally fall within the following categories: talent acquisition, time and labor management, payroll, talent management and HR management.

Talent Acquisition

Applicant Tracking. Our applicant tracking application simplifies the recruiting processes needed to hire the most qualified employees. By using our all-in-one system, our clients can move candidates from the application process through new employee on-boarding without re-keying data. Organizations can maintain and easily access a list of potential employees from a talent pool with real-time candidate, recruiter and manager retrieval while eliminating manual redundancies. Clients can also distribute job openings and reach a wider candidate audience with tools to reach unlimited postings on a network of free job boards and manage fee-based job board accounts.

Candidate Tracker. Our candidate tracker application enables recruiters to track and stay connected to potential talent through an online database of top candidates. This application helps clients fill future positions faster and without the cost of professional recruiting firms. This feature allows clients to assemble a contact history searchable by school, degree, skill set, previous employer, ZIP code radius and follow-up date.

Background Checks. Our background check application helps to ensure that prospective new hires are qualified candidates. Our application helps businesses perform instantaneous background checks where employers can choose the specific types of searches and how the screening results are issued. Additionally, employers are able to run background checks on existing employees at any time.

On-Boarding. Our on-boarding application streamlines the hiring and termination processes for employees of our clients by creating online checklists of tasks to be assigned to an employee or group of employees. With our application, this process can begin even before a new hire's first day on the job, helping the new hire be more productive on his or her first day.

E-Verify ®. By allowing electronic signature verification and online storage, our E-Verify ® application automates employment verification and reduces our clients' exposure to audits and penalties that could result from I-9 violations.

Tax Credit Services. Our tax credit services application helps employers process and calculate the available federal tax credits associated with hiring employees who meet various qualifications, ensuring organizations opting into this service receive their share of government-appropriated funds. This application prescreens candidates to determine who is eligible for tax credits.

Time and Labor Management

Time and Attendance. Our time and attendance application allows our clients to accurately and efficiently manage when, where and how employees report their hours worked. Clients can apply customized rules, use batch editing and use timecard management tools to manage complex time and attendance needs. Employees can clock in and out at their desks with web-based time clocks or by using biometric, badgeswipe or other types of hardware terminals in a single or multiclock environment. Our web time clock feature allows employees to clock in and out using their mobile device or any device with an internet connection, which automatically updates the payroll application when approved, eliminating the need to manually calculate timesheets and re-key information into payroll systems.

Scheduling/Schedule Exchange. Our scheduling application helps managers with employee scheduling through automated functionality that provides for a seamless workflow with the payroll and time and attendance applications. This application allows clients to create and edit templates for different pay classes.

Our schedule exchange application allows employees and managers access to their schedules at any time and employees can approve, decline or swap their schedules and see what shifts are available for pickup. Email notifications are sent automatically to supervisors and employees when schedules are created, requests for shift exchanges are submitted or a shift change is approved or denied.

Time-Off Requests. Our time-off requests application automates and standardizes the time-off request procedure and helps employers remain effectively staffed. Managers can view an online time-off calendar to easily monitor and approve or deny time-off requests. Managers can review paid time off requests via email and approve or deny such requests with ease. Our employee self-service tool allows employees to view the time-off they have available, submit requests and view blackout dates, the status of requests and any manager comments.

Labor Allocation. Our labor allocation application simplifies the process of setting up and tracking employee hours based on the job the employee is working.

Labor Management Reports/Push Reporting. Our labor management reports application provides clients with access to up-to-the-minute reports on the information they need to better manage their labor force, such as overtime and labor distribution. Our push reporting application also gives clients the ability to set up recurring reports and to schedule them to be run automatically and sent to users on a daily, weekly, monthly, quarterly or yearly basis.

Geofencing/Geotracking. Enhancing our time and attendance solution, Paycom’s geofencing and geotracking location-based technology assist our clients in managing the whereabouts of employees while on the job. Geofencing allows employers to establish geographical boundaries within which their employees are authorized to clock in and out when using our web time clock on smartphones, tablets or other electronic devices. Once enabled, this time-theft-combatting tool supersedes IP address restrictions, meaning the system first checks for authorized geographical locations, rather than authorized IP addresses. In addition, the geotracking tool empowers clients to track employees’ geographical locations upon clocking in and out. The coordinates collected by the application can be entered into and viewed on a Google® display map.

Payroll

Payroll and Tax Management. Our payroll application is the foundation of our solution and all of our clients are required to utilize this application in order to access our other applications. Our payroll application is automatically updated with changes in employee information and offers other time saving functionality such as batch editing and effective dating. Enhanced payroll grid functionality allows clients to automate and delegate payroll functions to accelerate the processes, giving clients repeatable, reliable payroll processing with additional controls. The application can be accessed at any time to make changes, run payroll and generate custom reports. We also help our clients by handling their payroll taxes and deposits, regulatory correspondence and amendments as well as assisting with penalty and interest disputes.

Paycom Pay. Our Paycom pay application eliminates the tedious, risky job of check reconciliation by issuing checks to our clients' employees that clear from a Paycom bank account, which helps clients eliminate potential liability and simplifies the reconciliation process. This helps reduce the number of transaction on a client's general ledger and simplifies bank statement balancing.

Expense Management. Our expense management application eliminates the manual, paper-based processes associated with employee expense reimbursement and allows employers to control and monitor expenses by setting clearly defined rules and parameters for employee reimbursement. Employees can upload receipts when submitting their expenses and access an expense dashboard where they can view the status of their submitted expenses through Employee Self-Service. Organizations gain audit-ready reporting, which is critical when a client needs to know who approved or denied a request, when and more.

Mileage Tracker/FAVR. Our native mobile app includes mileage tracker capability, allowing employers to more accurately track, log and manage employees' mileage reimbursements that are then automatically updated within our expense management applications. FAVR, which stands for Fixed and Variable Rate, allows our clients to customize their mileage reimbursement rate, according to IRS guidelines, to ensure accurate employee reimbursement for business miles without overpaying on reimbursements.

Garnishment Management. Our garnishment management application mitigates the risk of penalties and lawsuits from employees and agencies, allowing clients to handle communications with garnishment payees and agencies and to calculate and track garnishment payments.

GL Concierge. Our GL concierge application offers organizations more control and transparency into their payroll general ledger and gives finance professionals intuitive reporting, enriched audit trails, customizable file layouts and real-time alerts. Clients of all sizes can utilize a wide variety of general ledger maps along with an action-item alert system that improves the dynamics of their daily operations. With this simplified process, accounting departments can generate mapped GL reports for direct import into various accounting software packages.

Talent Management

Employee Self-Service. Available in English or Spanish, our employee self-service application improves employee engagement by empowering employees to self-manage certain transactions, obtain quick answers to frequent payroll and HR questions, access their pay history, view performance goals and reviews and view total compensation reports that show their compensation and benefits package. Benefits information and paid time-off accruals also give employees the ability to make informed decisions regarding their benefit selections and time-off requests. Employees can access our self-service software through any device with an internet connection or by downloading the Paycom app on the Google Play™ store and the App Store® online store.

Compensation Budgeting. Our compensation budgeting application provides compensation and performance information in one system, providing clients valuable workforce insight to help manage and formulate salary budgets and establish merit-based compensation increases that automatically upload new rates to payroll once the merit increases are set. Having payroll linked with performance reviews is instrumental for compensation budgeting, which rewards employees fairly while staying within budget.

Performance Management. Our performance management application allows employees to set standardized pay grades and performance goals for positions across an organization, helping align company goals with workforce goals. It also helps streamline the performance review process with online facilitation of the review process and links performance to pay.

My Analytics. The my analytics application offers powerful workforce insight in a variety of report formats. Because we offer an all-in-one solution in a single-database, the comprehensive report data provides the workforce intelligence needed to drive human capital decisions at all levels of management.

As part of the my analytics application, we offer employment predictor reporting. This sophisticated machine learning technology gives an employer greater insight into employees at risk of leaving its organization.

Paycom Learning and Course Content. Our learning management application formalizes and standardizes our clients' training processes. Employers can create customized content utilizing videos, presentations, quizzes and surveys. It provides employees with "anytime, anywhere" access to a central knowledge base where the employee can access content, share expertise and measure his or her professional development progress. Employers gain comprehensive reporting insights by running custom or predefined reports, including pass versus. fail and quiz statistics.

In addition to providing the ability to create and upload custom content, we created and launched our own proprietary eLearning content. Paycom Learning clients have immediate access to a library of Paycom-created learning courses, which allow employers to educate their managers and employees quickly and consistently on foundational topics such as workplace violence, discrimination and harassment prevention.

HR Management

Document and Checklist. Our document and checklist application is designed to manage employee files and allows employees to digitally sign and view company documents. We securely store client records to meet retention requirements and protect documents from unauthorized access and other disasters that can threaten businesses. Aside from expending fewer resources on paper, printing and file storage, our document and checklist application protects sensitive information and documents by customizing user access levels. In addition, clients can assign checklists to employees for the completion of certain tasks associated with processes such as on-boarding and off-boarding.

Government and Compliance. Our government and compliance application helps clients reduce exposure to violations, audits and penalties with respect to the employment laws impacting their business, such as the Fair Labor Standards Act, Family Medical Leave Act, Equal Employment Opportunity Act, COBRA and other state and federal regulations. A single-database keeps our clients' employee data consistent and enhances reporting capabilities by providing better accuracy and real-time insight.

Benefits Administration/Benefits to Carrier. Our benefits administration application allows clients to customize benefit plan setup, deduction amounts, enrollment dates and new-hire waiting periods. Employers are provided census and reconciliation reports to ensure they do not overpay for benefits. Employers can also update deduction amounts for all employees or groups of employees at once and automatically updates all insurance carriers for any changes. This application also provides employees with online enrollment and helps educate them by allowing them to view per-pay-period deduction amounts and preview how these deductions would affect their take-home pay, driving better informed enrollment decisions for greater employee satisfaction. Our benefits to carrier application automatically updates insurance carriers regarding benefit deduction amounts, address changes, termination of benefits and qualifying events.

COBRA Administration. Our COBRA administration application helps protect employers from COBRA violations and the associated fines and penalties by automatically initiating compliance measures upon entry of qualifying events into the application. In addition to sending required correspondence, this application also tracks important dates, collects and remits premiums and reports on all COBRA activity.

Personnel Action Forms. Our personnel action forms application helps our clients reduce the amount of time and paperwork required to make employee changes, such as pay rate, position and title changes, by allowing managers to complete and approve online personnel action forms, subject to necessary approvals from the HR department. This feature reduces errors and eliminates re-keying of data and even feeds to payroll with an effective date.

Surveys. Our surveys application allows employers to conduct confidential email surveys of employees on workplace matters, providing employers with candid feedback that otherwise may go undisclosed. From exit interviews and benefits assessments to rate-the-boss questionnaires, this valuable information can be used to drive decisions and realize company goals. Clients can analyze results by the demographics of the workforce and compare how results change over time.

Enhanced ACA. Our Affordable Care Act (“ACA”) application provides clients with access to a dashboard that tracks employee count, employee status, health care plan affordability and ACA periods all from one convenient location and enables Paycom to file IRS Forms 1094/1095-B and/or –C. Clients utilizing this application also have access to additional real-time compliance reports, alerts and historical data for audit trail purposes.

Our Clients

We serve a diverse client base in terms of size and industry. We have over 23,500 clients, or approximately 12,700 clients based on parent company grouping, none of which constituted more than one-half of one percent of our revenues for the year ended December 31, 2018. We stored data for over 4.1 million persons employed by our clients during the year ended December 31, 2018.

Many small to mid-sized companies can typically make the decision to adopt our solution more quickly than larger companies, which we believe results in a shorter sales cycle and more closely corresponds to our target sales cycle of 30 to 90 days. As a result of the nature and size of our clientele, we maintain a diversified client base and very low revenue concentration among our clients. We believe, however, that larger employers represent a substantial opportunity to increase the number of clients we serve and to increase our revenues per client with limited incremental cost. As we attract clients at the higher end of our target client size range, we may face longer sales cycles and less predictability in completing some of our sales.

Competition

The market for HCM solutions is rapidly evolving, highly competitive and subject to changing technology, shifting client needs and frequent introduction of new products and services. Our competitors range from small, regional firms to large, well-established international firms with multiple product offerings.

We compete with firms that provide HCM solutions by various means. Many providers continue to deliver legacy enterprise software, but as demand for greater flexibility and access to information grows, we believe there will be increased competition in the delivery of HCM cloud-based solutions by other SaaS providers. Our competitors offer HCM solutions that may overlap with one, several or all categories of applications offered by our solution. Our talent acquisition and talent management applications compete primarily with Cornerstone OnDemand, Inc., Oracle Corporation, SAP SE and Workday, Inc. Our payroll applications, including payroll processing, compete primarily with Automatic Data Processing, Inc. (“ADP”), Ceridian HCM, Inc. (“Ceridian”), Paychex, Inc., Paylocity Holding Corporation and The Ultimate Software Group, Inc. Our HR management applications compete primarily with ADP, Ceridian, Oracle Corporation, Paychex, Inc., Paylocity Holding Corporation, SAP SE and Workday, Inc. Our time and labor management applications compete primarily with ADP, Ceridian, Kronos Incorporated, Paylocity Holding Corporation and The Ultimate Software Group, Inc. Our larger competitors compete with us across multiple segments. In addition, our HCM solution continues to face competition from in-house payroll and HR systems and departments as well as HR systems and software sold by third-party vendors.

Competition in the HCM solutions market is primarily based on service responsiveness, product quality and reputation, breadth of service, application offering and price. The importance of these factors depends on the size of the business. Price tends to be the most important factor of competition for smaller businesses with fewer employees, while the scope of features and customization is more important to larger businesses. Regardless of a company’s size, another important factor is the implementation experience, as all organizations are seeking a streamlined and simplified process.

Sales and Marketing

We sell our solution exclusively through our captive sales force, substantially all of whom have a four-year college degree. We typically recruit sales candidates who have sales experience in non-HCM industries or, with respect to candidates recruited directly from colleges and universities, who have demonstrated an aptitude for sales. Our sales force is comprised of inside sales and field sales personnel, who are organized geographically, and client relations representatives ("CRRs"), who sell additional applications to existing clients. As of the filing of this Form 10-K, we have 49 sales teams located in 26 states and plan to open additional sales offices to further expand our presence in the U.S. market.

We provide our sales force with an intensive eight-week training course that includes at least one week of training at our headquarters in Oklahoma City. Our unique training program includes instruction in accounting, business metrics, application features and tax matters relevant to our target market and we believe it fosters loyalty and helps maintain our corporate culture. Our training continues for our sales force through weekly in-office strategy sessions and leadership development training. Executive sales representatives are also required to attend in-person quarterly conferences to share best practices and receive legal and business updates.

When a new client processes payroll with us for an entire month, our sales representative receives a one-time commission based upon an estimate of future annual revenues from such client. When an existing client purchases and then utilizes a new application for one payroll cycle, a CRR receives a one-time commission based upon an estimate of future annual revenues from such client. Executive sales representatives receive a higher commission rate and base salary based upon both current year and life-to-date realized sales.

We generate client leads, accelerate sales opportunities and build brand awareness through our marketing programs that target senior finance and HR executives, technology professionals and senior business leaders of companies that perform HCM functions in-house or outsource these functions to one of our competitors. Our marketing programs include:

- Podcasts, webinars, blogs, white papers and infographics;
- National and local television advertising campaigns, personalized direct mail campaigns, email campaigns, social and digital media campaigns, industry-specific advertising and tradeshow exhibiting; and
- Search engine marketing methods that include site optimization and pay-per-click searches.

In addition to managing client relationships, our CRRs are focused on expanding the number of applications our clients purchase from us by introducing them to additional applications. Our CRRs call upon select clients periodically and are paid a non-recurring commission on any additional sales they generate.

Technology, Operations and Security

Technology

Our multi-tenant architecture enables us to deliver our solution across our client base with a single instance of our solution, while securely partitioning access to our clients' respective application data. Because a single version of our solution is developed, supported and deployed across all of our clients, updates are delivered to all of our clients at the same time, making it easier to scale our solution as our number of clients and their respective employee headcounts increase.

We maintain multiple load-balanced internet lines serviced by multiple networks to provide our clients continuous access to our solution and their stored data. We back up our client data at regular intervals utilizing live replication, snapshots and cold archive methods of backup and manually monitor backup success and failure regularly. Our server cluster and database servers have redundant "hot swappable" disks to ensure continuous service in the event of a disk failure.

Operations

We physically host our solution for our clients in three secure data center facilities located in Oklahoma and Texas. All of our critical systems are fully redundant and backed-up in real-time to these facilities. Physical security includes ID-oriented access control, alarm systems and manned 24-hour-a-day camera monitoring by our security guards. Server facilities also have environmental monitoring and extensive environmental controls such as heat and fire protection, moisture, temperature, and humidity sensors, backup power supply and exterior reinforced concrete walls.

Security

We maintain a formal and comprehensive security program designed to ensure the confidentiality, integrity and availability of our clients' data. During the regular course of business, we receive client data through our online system that we in turn process, record and store following ISO/IEC 270001:2013 certified controls and procedures. All communications with our servers that might contain sensitive information are encrypted before they leave the network and our servers are configured to only allow high-grade encryption algorithms.

We strictly regulate and limit all access to servers and networks at each of our facilities. Local network access is restricted by our authenticated server, using access control lists and remote network access is restricted by a firewall, which provides no accessible route from external networks to systems within our local network. We also employ network and host intrusion detection and prevention sensors throughout our infrastructure, systems that monitor that infrastructure and alert our security department of cybersecurity issues, a system for managing and installing patches for unsecure third-party applications and highly restricted access to the internet for anyone who has access to client data. Our information security department regularly performs penetration testing and we retain a third-party penetration testing company to conduct penetration tests and periodic audits to identify and remediate any issues.

Our applications are secured using multiple libraries and secure coding practices. Our IT infrastructure is secured and monitored using a number of best practices and tools at multiple layers of the physical and logical network. This security is also continually monitored by our information security department. All of our operations employees work in either our Oklahoma or Texas locations and, with the exception of certain IT personnel, are not permitted to work remotely.

Software Development

Our application development team works closely with our clients to enhance our existing application offerings and develop new applications. This process is led by experienced product managers who oversee the evolution of their respective applications within a focused timeframe of innovation and cultivation in order to deliver the well-developed applications and enhancements desired by our clients. Our product managers, many of whom are former HR executives, are proactive in their approach to assigning development requests based on research, trends and user feedback. A key element of our development process is the one-on-one personal interaction between clients and our CRRs, through whom our clients personally suggest new applications and features.

We develop our solution from the “ground up” with our internal development and engineering teams. Our development and engineering teams and our employees conceive new applications and enhancements, review requests, schedule development in order of priority and subsequently develop the applications or enhancements. Our new applications and enhancements are independently reviewed by the quality assurance team, in accordance with our software development process, before being fully implemented. Any enhancements to our applications are released on a monthly scheduled release date to coordinate the communication and release to our clients.

Capitalized software development expenses, which include compensation for employees directly associated with development projects, were $22.0 million, $15.8 million and $8.8 million for the years ended December 31, 2018, 2017 and 2016, respectively.

Client Service

We are committed to providing industry-leading, client-centered service. For this reason, we assign each client a specialist within a dedicated team. This one-on-one service is a key part of our client service model and helps to ensure we are delivering an industry-leading solution and maintaining high client satisfaction. The primary elements of our client service model include the following:

Streamlined Setup and On-Boarding

After electing to deploy our solution, a new client begins our on-boarding process with assistance from a team of new client setup specialists and the sales representative responsible for obtaining the client’s business. In addition, we also have a team of transition specialists whose job it is to ensure that the process is performed smoothly, data is collected properly and all relevant employees are fully trained on the system. This team works closely with the client until the client is capable of managing our solution independently, at which time responsibility for the client relationship is transferred to our dedicated CRRs and service specialists. Unlike certain of our competitors, we do not outsource any of our on-boarding efforts.

Dedicated Service Specialists

After completing the on-boarding process, each client is assigned to a services specialist within a dedicated team. Clients can then contact their dedicated services specialist or a team member if any issues or questions arise. These specialists provide personalized service with actual knowledge of the clients’ business needs. When appropriate, client questions can be elevated to the specialists with the appropriate application, regulatory or tax expertise. In addition, our CRRs proactively contact our clients to ensure satisfaction with our solution and introduce additional applications.

Expert Level Service

Our client specialists are trained across all of our applications to ensure that they can provide comprehensive, expert-level service. Our client service is ISO 9001:2015 certified and helps support our high client retention rate.

Regulatory and Certifications

We are subject to varying degrees of regulations in each of the jurisdictions in which we provide services. Local laws and regulations, and their interpretation and enforcement, differ significantly among those jurisdictions. These regulations and laws cover, among others, information privacy.

Data privacy has become a significant issue in the United States and in other countries. The regulatory framework for privacy issues worldwide is rapidly evolving and is likely to remain uncertain for the foreseeable future. Many federal, state and foreign government bodies and agencies have adopted or are considering adopting laws and regulations affecting or regarding the collection, use and disclosure of personal information. In the United States, these include, for example, rules and regulations promulgated under the authority of the Federal Trade Commission, the Health Insurance Portability and Accountability Act of 1996, the Family Medical Leave Act of 1993, the ACA and state breach notification laws. Further, because some of our clients have establishments in the European Union, the European Union's General Data Protection Regulation ("GDPR") may impact our processing of certain client and employee information.

We voluntarily obtain third-party security examinations relating to our internal controls over financial reporting in accordance with System and Organization Controls Report, I ("SOC 1"). Our SOC 1 examination is conducted every six months by one of the four largest independent international auditing firms, and addresses, among other areas, our physical and environmental safeguards for production data centers, data availability and integrity procedures, change management procedures and logical security procedures.

In October 2016, we renewed a certification based on ISO/IEC 27001:2013 criteria, a security standard for Information Security Management Systems published by ISO covering our production, quality assurance and implementation environments. This independent assessment of our conformity to the ISO 27001 standard includes assessing security risks, designing and implementing comprehensive security controls and adopting an information security management process to meet security needs on an ongoing basis. The certification is valid until December 2019, with continuing assessments taking place annually.

In April 2017, we renewed a certification based on ISO 9001:2015 criteria, a standard for the implementation of quality management processes published by ISO, covering our activities required to create and deliver our solution. This independent assessment of our conformity to the ISO 9001:2015 standard includes assessing the design and implementation of quality objectives to meet delivery standards on an ongoing basis. The certification is valid until April 2020, with continuing assessments taking place annually.

Intellectual Property

We rely on a combination of copyrights, trademarks, service marks, trade secret laws and contractual restrictions to establish and protect our intellectual property rights. We also have a number of registered and unregistered trademarks and will continue to evaluate the registration of additional trademarks as appropriate. We do not have any patents or patent applications pending.

Seasonality

Our revenues are seasonal in nature. Recurring revenues include revenues related to the annual processing of payroll forms, such as Form W-2 and Form 1099, and revenues from processing unscheduled payroll runs (such as bonuses) for our clients. Because payroll forms are typically processed in the first quarter of the year, first quarter revenues and margins are generally higher than in subsequent quarters. Further, beginning in the first quarter of 2016, we began generating additional revenues as a result of the enactment of the ACA, as many clients began complying with filing requirements for Forms 1094 and 1095. We anticipate that our revenues will continue to exhibit this seasonal pattern related to ACA form filings for so long as the ACA (or replacement legislation) includes employer reporting requirements. In addition, we often experience increased revenues during the fourth quarter due to unscheduled payroll runs for our clients that occur before the end of the year. Therefore, we expect the seasonality of our revenue cycle to decrease to the extent clients utilize more of our non-payroll applications.

Employees

Our ability to recruit and retain qualified employees is critical to our continued success. We invest heavily in our training and leadership development programs to encourage the development and promotion of our employees. As of December 31, 2018, we employed 3,050 people, substantially all of which are full-time. None of our employees were covered by collective bargaining agreements.

Facilities

Our corporate headquarters is an approximately 500,000-square-foot campus located on over 30 acres of Company-owned property in Oklahoma City, Oklahoma. In addition to housing two fully redundant data centers at our corporate headquarters, we operate another fully redundant data center at a leased property near Dallas, Texas. We plan to relocate our Texas operations, including the data center, to a new, expanded facility in Grapevine, Texas. We also lease a disaster recovery site in downtown Oklahoma City.

We also lease offices in Arizona, California, Colorado, Connecticut, Florida, Georgia, Illinois, Indiana, Maryland, Massachusetts, Michigan, Minnesota, Missouri, New Jersey, New York, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Tennessee, Texas, Utah, Virginia, Washington and Wisconsin. We believe that these facilities are suitable for our current operations and upon the expiration of the terms of the leases we believe we could renew these leases or find suitable space elsewhere on acceptable terms.

Segment Information

We operate in a single operating segment and a single reporting segment. Operating segments are defined as components of an enterprise about which separate financial information is regularly evaluated by the chief operating decision maker function (which is fulfilled by our chief executive officer) in deciding how to allocate resources and in assessing performance. Our chief executive officer allocates resources and assesses performance based upon financial information at the consolidated level. Since we operate in one operating segment, all required financial segment information is presented in the consolidated financial statements.

Available Information

Our internet address is www.paycom.com and our investor relations website is located at investors.paycom.com. Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports can be found on our investor relations website, free of charge, as soon as reasonably practical after we electronically file such material with, or furnish it to, the SEC. Information contained on our website is not incorporated by reference into this Form 10-K. The SEC maintains a public website, www.sec.gov, which includes information about and the filings of issuers that file electronically with the SEC.

Item 1A. Risk Factors
The risk factors noted in this section and other factors noted throughout this Form 10-K, including those risks identified in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," describe examples of risks, uncertainties and events that may cause our actual results to differ materially from those contained in any forward-looking statement. If one or more of these risks or uncertainties materialize, or if underlying assumptions prove incorrect, actual outcomes may vary materially from those included in this Form 10-K.

Changes in laws, government regulations and policies could have a material adverse effect on our business and results of operations.

Many of our applications are designed to assist our clients in complying with government regulations that continually change. The introduction of new regulatory or licensing requirements, or new interpretations of existing laws or regulations, could increase our cost of doing business. Changing regulatory requirements may make the introduction of new applications and enhancements more costly or more time-consuming than we currently anticipate or could prevent the introduction of new applications and enhancements by us altogether. Changes in laws, regulations or policies could also affect the extent and type of benefits employers are required, or may choose, to provide employees or the amount and type of taxes employers and employees are required to pay. Such changes could reduce or eliminate the need for certain of our existing applications, which would result in decreased revenues. Further, we may spend time and money developing new applications and enhancements that, due to regulatory changes, become unnecessary prior to being released. In addition, any failure to educate and assist our clients with respect to new or revised legislation that impacts them could have an adverse effect on our reputation, and any failure to modify our applications or develop new applications in a timely fashion in response to regulatory changes could have an adverse effect on our business and results of operations.

In addition, the future success of our business depends upon the continued use of the internet as a primary medium for commerce, communication and business. Federal, state and foreign government bodies or agencies have in the past adopted, and may in the future adopt, laws or regulations affecting the use of the internet as a commercial medium. Changes in these laws or regulations could require us to modify our applications. Further, government agencies or private organizations may impose taxes, fees or other charges for accessing the internet or commerce conducted via the internet. These laws or charges could limit the growth of internet-related commerce or communications generally or could result in reductions in the demand for internet-based applications such as ours.

If our security measures are breached, or unauthorized access to our clients' or their employees' sensitive data is otherwise obtained, our solution may not be perceived as being secure, clients may reduce the use of or stop using our solution, our ability to attract new clients may be harmed and we may incur significant liabilities.

Our solution involves the collection, storage and transmission of clients' and their employees' confidential and proprietary information, including personal identifying information, as well as financial and payroll data. HCM software is often targeted in cyber-attacks, including computer viruses, worms, phishing attacks, malicious software programs and other information security breaches, which could result in the unauthorized release, gathering, monitoring, misuse, loss or destruction of our clients' sensitive data or otherwise disrupt our clients' or other third parties' business operations. If cybercriminals are able to circumvent our security measures, or if we are unable to detect an intrusion into our systems and contain such intrusion in a reasonable amount of time, our clients' sensitive data may be compromised.

Certain of our employees have access to sensitive information about our clients' employees. While we conduct background checks of our employees and limit access to systems and data, it is possible that one or more of these individuals may circumvent these controls, resulting in a security breach.

Although we have security measures in place to protect client information and prevent data loss and other security breaches, these measures could be breached as a result of third-party action, employee error, malfeasance or otherwise. Because the techniques used to obtain unauthorized access or to sabotage systems change frequently, we may not be able to anticipate these techniques and implement adequate preventative or protective measures. While we currently maintain a cyber liability insurance policy, cyber liability insurance may be inadequate or may not be available in the future on acceptable terms, or at all. In addition, our cyber liability insurance policy may not cover all claims made against us, and defending a suit, regardless of its merit, could be costly and divert management's attention from our business and operations.

Any actual or perceived breach of our security could damage our reputation, cause existing clients to discontinue the use of our solution, prevent us from attracting new clients, or subject us to third-party lawsuits, regulatory fines or other actions or liabilities, any of which could adversely affect our business, operating results or financial condition.

Any damage, failure or disruption of our SaaS network infrastructure or data centers could impair our ability to effectively provide our solution, harm our reputation and adversely affect our business.

Our SaaS network infrastructure is a critical part of our business operations. Our clients access our solution through standard web browsers, smart phones, tablets and other web-enabled devices and depend on us for fast and reliable access to our solution. We serve all of our clients from our three fully redundant data centers located in Oklahoma and Texas. Our SaaS network infrastructure and data centers are vulnerable to damage, failure and disruption.

In the future, we may experience issues with our computing and communications infrastructure or data centers caused by the following factors:

- human error;
- telecommunications failures or outages from third-party providers;
- computer viruses or cyber-attacks;
- break-ins or other security breaches;
- acts of terrorism, sabotage, intentional acts of vandalism or other misconduct;
- tornadoes, fires, earthquakes, hurricanes, floods and other natural disasters;
- power loss; and
- other unforeseen interruptions or damages.

If our SaaS network infrastructure or our clients' ability to access our solution is interrupted, client and employee data from recent transactions may be permanently lost, and we could be exposed to significant claims by clients, particularly if the access interruption is associated with problems in the timely delivery of funds payable to employees. Further, any adverse changes in service levels at our data centers resulting from damage to or failure of our data centers could result in disruptions in our services. Any significant instances of system downtime or performance problems at our data centers could negatively affect our reputation and ability to attract new clients, prevent us from gaining new or additional business from our current clients, or cause our current clients to terminate their use of our solution, any of which would adversely impact our revenues. In addition, if our network infrastructure and data centers fail to support increased capacity due to growth in our business, our clients may experience interruptions in the availability of our solution. Such interruptions may reduce our revenues, cause us to issue refunds to clients or adversely affect our retention of existing clients, any of which could have a negative impact on our business, operating results or financial condition.

Privacy concerns and laws or other regulations may reduce the effectiveness of our applications.

Our applications are subject to various complex laws and regulations on the federal, state and local levels, including those governing data privacy, which has become a significant issue globally. The regulatory framework for privacy issues is rapidly evolving and is likely to remain uncertain for the foreseeable future. Many federal, state and foreign government bodies and agencies have adopted or are considering adopting laws and regulations regarding the collection, use and disclosure of personal information. In the United States, these include rules and regulations promulgated under the authority of the Federal Trade Commission, the Health Insurance Portability and Accountability Act of 1996, the Family Medical Leave Act of 1993, the ACA, federal and state labor and employment laws and state data breach notification laws. Further, because some of our clients have establishments in the European Union, GDPR may impact our processing of certain client and employee information. Failure to comply with privacy laws and regulations could result in the imposition of consent orders or civil and criminal penalties, including fines, which could damage our reputation and have an adverse effect on our results of operations or financial condition.

In addition to government regulation, privacy advocates and industry groups may propose new and different self-regulatory standards. Because the interpretation and application of privacy and data protection laws are still uncertain, it is possible that these laws may be interpreted and applied in a manner that is inconsistent with our existing data management practices or the features of our solution. Any failure to comply with government regulations that apply to our applications, including privacy and data protection laws, could subject us to liability. In addition to the possibility of fines, lawsuits and other claims, we could be required to fundamentally change our business activities and practices or modify our solution, which could have an adverse effect on our business, operating results or financial condition. Any inability to adequately address privacy concerns, even if unfounded, or comply with applicable privacy or data protection laws, regulations and policies, could result in additional cost and liability to us, damage our reputation, inhibit sales and adversely affect our business, operating results or financial condition.

Furthermore, privacy concerns may cause our clients' employees to resist providing the personal data necessary to allow our clients and their employees to use our applications effectively. Even the perception of privacy concerns, whether or not valid, may inhibit market adoption of our applications in certain industries. All of these legislative and regulatory initiatives may adversely affect the ability of our clients to process, handle, store, use and transmit demographic and personal information from their employees, which could reduce demand for our solution.

The market in which we participate is highly competitive, and if we do not compete effectively, our business, operating results or financial condition could be adversely affected.

The market for HCM software is highly competitive, rapidly evolving and fragmented. We expect competition to intensify in the future with the introduction of new technologies and new market entrants. Many of our current and potential competitors are larger and have greater brand name recognition, longer operating histories, more established relationships in the industry and significantly greater financial, technical and marketing resources than we do. As a result, some of these competitors may be able to:

- adapt more rapidly to new or emerging technologies and changes in client requirements;
- develop superior products or services, gain greater market acceptance and expand their product and service offerings more efficiently or rapidly;
- bundle products and services that we may not offer or in a manner that provides them with a price advantage;
- take advantage of acquisition and other opportunities for expansion more readily;
- maintain a lower cost basis;
- adopt more aggressive pricing policies and devote greater resources to the promotion, marketing and sale of their products and services; and
- devote greater resources to the research and development of their products and services.

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

We compete with firms that provide HCM solutions by various means. Our competitors offer HCM solutions that overlap with one, several or all categories of applications that we offer. Our talent acquisition and talent management applications compete primarily with Cornerstone OnDemand, Inc., Oracle Corporation, SAP SE and Workday, Inc. Our payroll applications, including payroll processing, compete primarily with ADP, Ceridian, Concur Technologies, Inc., Intuit Inc., Paychex, Inc., Paylocity Holding Corporation and The Ultimate Software Group, Inc. Our HR management applications compete primarily with ADP, Ceridian, Oracle Corporation, Paychex, Inc., Paylocity Holding Corporation, SAP SE, and Workday, Inc. Our time and labor management applications compete primarily with ADP, Ceridian, Kronos Incorporated, Paylocity Holding Corporation and The Ultimate Software Group, Inc. Most of our larger competitors compete with us across multiple application categories. In addition, our HCM solution continues to face competition from in-house payroll and HR systems as well as HR systems and software sold by third-party vendors.

Competition in the HCM solutions market is primarily based on service responsiveness, application quality and reputation, breadth of service and product offering and price. Many of our competitors have established marketing relationships, access to larger client bases and major distribution agreements with consultants, software vendors and distributors. In addition, some competitors may offer software that addresses one or a limited number of HCM functions at a lower price point or with greater depth than our solution. Further, some potential clients, particularly large enterprises, may elect to develop their own internal solutions. If we are unable to compete effectively, our business, operating results or financial condition could be adversely affected.

The adoption of new, or adverse interpretations of existing, state and federal money transmitter or money services business statutes could subject us to additional regulation and related expenses and require changes to our business.

The adoption of new money transmitter or money services business statutes in jurisdictions, changes in regulators' interpretation of existing state and federal money transmitter or money services business statutes or regulations, or disagreements by regulatory authorities with our interpretation of such statutes or regulations, could subject us to registration or licensing or limit business activities until we are appropriately licensed. These occurrences could also require changes to the manner in which we conduct certain aspects of our business or invest client funds, which could adversely impact the amount of interest income we receive from investing client funds before such funds are remitted to the appropriate taxing authorities and accounts designated by our clients.

While we maintain that we are not a money services business or money transmitter, we have adopted an anti-money laundering ("AML") compliance program to mitigate the risk of our application being used for illegal or illicit activity and to help detect and prevent fraud. Our AML compliance program is designed to foster trust in our application and services.

Recently, we were required to register as a "money services business" in one jurisdiction. Should other state or federal regulators make a determination that we have operated as an unlicensed money services business or money transmitter, we could be subject to civil and criminal fines, penalties, costs of registration, legal fees, reputational damage or other negative consequences, all of which may have an adverse effect on our business operating results or financial condition.

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

Our results of operations, including our revenues, costs of revenues, administrative expenses, operating income, cash flow and deferred revenue, may vary significantly in the future, and the results of any one period should not be relied upon as an indication of future performance. Fluctuations in our financial results may negatively impact the value of our common stock. Our financial results may fluctuate as a result of a variety of factors, many of which are outside of our control, and as a result, may not fully reflect the underlying performance of our business. Factors that may cause our financial results to fluctuate from period to period include, without limitation:

- our ability to attract new clients or sell additional applications to our existing clients;
- the number of new clients and their employees, as compared to the number of existing clients and their employees in a particular period;
- the mix of clients between small, mid-sized and large organizations;
- the extent to which we retain existing clients and the expansion or contraction of our relationships with them;
- the mix of applications sold during a period;
- changes in our pricing policies or those of our competitors;
- seasonal factors affecting payroll processing, demand for our applications or potential clients' purchasing decisions;
- the amount and timing of operating expenses, including those related to the maintenance and expansion of our business, operations and infrastructure;
- the timing and success of new applications introduced by us and the timing of expenses related to the development of new applications and technologies;
- the timing and success of current and new competitive products and services by our competitors;
- economic conditions affecting our clients, including their ability to outsource HCM solutions and hire employees;
- changes in laws, regulations or policies affecting our clients' legal obligations and, as a result, demand for certain applications;
- changes in the competitive dynamics of our industry, including consolidation among competitors or clients;
- our ability to manage our existing business and future growth, including expenses related to our data centers and the expansion of such data centers and the addition of new offices;
- the effects and expenses of acquisition of third-party technologies or businesses and any potential future charges for impairment of goodwill resulting from those acquisitions;
- inclement weather or natural disasters, including but not limited to tornadoes, hurricanes, fires, earthquakes and floods;
- network outages or security breaches; and
- general economic, industry and market conditions.

Our business and operations are experiencing rapid growth and organizational change. If we fail to manage such growth and change effectively, we may be unable to execute our business plan, maintain high levels of service or adequately address competitive challenges.

We have experienced, and may continue to experience, rapid growth in our headcount and operations, which has placed, and may continue to place, significant demands on our management, operational and financial resources. For example, our headcount has grown from 523 employees as of December 31, 2011 to 3,050 employees as of

December 31, 2018, and we have expanded from 20 sales teams as of December 31, 2011 to 49 sales teams as of the filing of this Form 10-K. We have also experienced significant growth in the number of clients and transactions and the amount of client and employee data that our infrastructure supports. Finally, our organizational structure and recording systems and procedures are becoming more complex as we improve our operational, financial and management controls. Our success depends, in part, on our ability to manage this growth and organizational change effectively.

To manage the expected growth of our headcount and operations, we must continue to improve our operational, financial and management controls and our reporting systems and procedures. The failure to effectively manage growth could result in declines in the quality of, or client satisfaction with, our applications, increases in costs, difficulties in introducing new applications or other operational difficulties, any of which could adversely affect our business by impairing our ability to retain and attract clients or sell additional applications to our existing clients.

Further, we need to continue to expand our sales force and support team members in order to grow our client base and increase our revenues, but our ability to add additional offices may be constrained by the willingness and availability of qualified personnel to staff and manage any new offices and our success in recruiting and training sales personnel in those new offices. If our expansion efforts are unsuccessful, our business, operating results or financial condition could be adversely affected.

Our business, operating results or financial condition could be adversely affected if our clients are not satisfied with our deployment or technical support services, or if our solution fails to perform properly.

Our business depends on our ability to satisfy our clients, both with respect to our applications and the technical support provided to help our clients use the applications that address the needs of their businesses. We use our in-house deployment personnel to implement and configure our solution and provide support to our clients. If a client is not satisfied with the quality of our solution, the applications delivered or the support provided, we could incur additional costs to address the situation, our profitability might be negatively affected, and the client's dissatisfaction with our deployment or support service could harm our ability to sell additional applications to that client. In addition, our sales process is highly dependent on the reputation of our solution and applications and on positive recommendations from our existing clients. Our clients have no obligation to continue to use our applications, and may choose not to continue to use our applications at the same or higher level of service, if at all. In the past, some of our clients have elected not to continue to use our applications. Moreover, our clients generally have the right to cancel their agreements with us for any or no reason by providing 30 days' prior written notice. Any failure to maintain high-quality technical support, or a market perception that we do not maintain high-quality technical support, could adversely affect client retention, our reputation, our ability to sell our applications to existing and prospective clients, and, as a result, our business, operating results or financial condition.

Further, our solution is inherently complex and may in the future contain, or develop, undetected defects or errors. Any defects in our applications could adversely affect our reputation, impair our ability to sell our applications in the future and result in significant costs to us. The costs incurred in correcting any application defects may be substantial and could adversely affect our business, operating results or financial condition. Any defects in functionality or that cause interruptions in the availability of our applications could result in:

- loss or delayed market acceptance and sales of our applications;
- termination of service agreements or loss of clients;
- credits or refunds to clients, including reimbursements for any fees or penalties assessed by regulatory agencies;
- breach of contract, breach of warranty or indemnification claims against us, which may result in litigation;
- diversion of development and service resources; and
- injury to our reputation.

Because of the large amount of data that we collect and manage, it is possible that hardware failures or errors in our applications could result in data loss or corruption or cause the information that we collect to be incomplete or contain inaccuracies that our clients regard as significant. Our clients might assert claims against us in the future alleging that they suffered damages due to a defect, error, or other failure of our solution. Our errors and omissions insurance may be inadequate or may not be available in the future on acceptable terms, or at all. In addition, our policy may not cover all claims made against us, and defending a suit, regardless of its merit, could be costly and divert management’s attention. Any failures in the performance of our solution could harm our reputation and our ability to retain existing clients and attract new clients, which would have an adverse impact on our business, operating results or financial condition.

If we are not able to develop enhancements and new applications, keep pace with technological developments or respond to future disruptive technologies, we might not remain competitive and our business could be adversely affected.

Our continued success will depend on our ability to adapt and innovate. In order to attract new clients and increase revenues from existing clients, we need to enhance, add new features to and improve our existing applications and introduce new applications. The success of any enhancements or new features and applications depends on several factors, including timely completion and   introduction and market acceptance. We may expend significant time and resources developing and pursuing sales of a particular enhancement or application that may not result in revenues in the anticipated time frame or at all, or may not result in revenue growth sufficient to offset increased expenses. Further, changing legal and regulatory requirements may delay the development or introduction of enhancements or new applications or render certain of our applications obsolete. If we are unable to successfully develop enhancements, new features or new applications to meet client needs, our business and operating results could be adversely affected.

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

Our success is also subject to the risk of future disruptive technologies. If new technologies emerge that are able to deliver HCM solutions at lower prices, more efficiently or more conveniently, such technologies could adversely impact our ability to compete.

The market for our solution among large companies may be limited if these companies demand customized features and functions that we do not offer.

Prospective clients, especially larger companies, may require customized features and functions unique to their business processes that we do not offer. In order to ensure we meet these requirements, we may devote a significant amount of support and service resources to larger prospective clients, increasing the cost and time required to complete sales with no guarantee that these prospective clients will adopt our solution. Further, we may not be successful in implementing any customized features or functions. If prospective clients require customized features or functions that we do not offer, or that would be difficult for them to deploy themselves, the market for our solution will be more limited and our business could be adversely affected.

We are dependent on the continued service of our key executives and, if we fail to retain such key executives, our business could be adversely affected.

We believe that our success depends in part on the continued services of our senior management team, consisting of Chad Richison, Craig E. Boelte, Jeffrey D. York, Jon Evans and Bradley S. Smith. Our business could be adversely affected if we fail to retain these key executives. Although the employment arrangements of certain of our key executives contain non-competition restrictions, our business could nonetheless be adversely affected if a key executive leaves Paycom and attempts to compete with us. In addition, we have not purchased key person life insurance on any members of our senior management team.

If we are unable to attract and retain qualified personnel, including software developers and skilled IT, sales and marketing personnel, our ability to develop and market new and existing products and, in turn, increase our revenue and profitability could be adversely affected.

Our future success is dependent on our ability to continue to enhance and introduce new applications. As a result, we are heavily dependent on our ability to attract and retain qualified software developers and IT personnel with the requisite education, background and industry experience. In addition, to continue to execute our growth strategy, we must also attract and retain qualified sales, marketing and operational personnel capable of supporting a larger and more diverse client base. The software industry is characterized by a high level of employee mobility and aggressive recruiting among competitors. This competition for qualified personnel may be amplified by new immigration laws or policies that could limit software companies' ability to recruit internationally. Although such changes in immigration laws or policies would not have a significant direct impact on our workforce, the ensuing increase in demand for software developers and IT personnel could impair our ability to attract or retain skilled employees and/or significantly increase our costs to do so. Furthermore, identifying and recruiting qualified personnel and training them in the use of our applications requires significant time, expense and attention, and it can take a substantial amount of time before our employees are fully trained and productive. The loss of the services of a significant number of employees could be disruptive to our development efforts, which may adversely affect our business by causing us to lose clients, increase operating expenses or divert management's attention to recruit replacements for the departed employees.

The failure to develop and maintain our brand cost-effectively could have an adverse effect on our business.

We believe that developing and maintaining widespread awareness of our brand in a cost-effective manner is critical to achieving widespread acceptance of our solution and is an important element in attracting new clients and retaining existing clients. Successful promotion of our brand depends largely on the effectiveness of our marketing efforts and on our ability to provide reliable and useful applications at competitive prices. Brand promotion activities may not yield increased revenues, and even if they do, any increased revenues may not offset the expenses incurred in building our brand. If we fail to successfully promote and maintain our brand, or incur substantial expenses in an unsuccessful attempt to promote and maintain our brand, we may fail to attract enough new clients or retain our existing clients to the extent necessary to realize a sufficient return on our brand-building efforts, which could have an adverse effect on our business.

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

We have historically experienced seasonality in our revenues because a significant portion of our recurring revenues relate to the annual processing of payroll forms such as Form W-2 and Form 1099 and, beginning in 2016, the annual processing and filing of

ACA-related forms. Because these forms are typically processed in the first quarter of the year, first quarter revenues are generally higher than revenues in subsequent quarters. In addition, unscheduled payroll runs at the end of the year (such as bonuses) often result in increased revenues in the fourth quarter. We expect this seasonality to continue in the future, although the repeal or modification of the ACA could have an impact on the seasonality of our revenues. Seasonal fluctuations in certain of our operating results and financial metrics may make such results and metrics difficult to predict.

The modification or repeal of certain provisions of the ACA could have an adverse effect on our business, financial condition and results of operations.

We generate ACA-related revenues (i) on an annual basis in connection with processing and filing Forms 1094 and 1095 on behalf of clients and (ii) from clients who have purchased our Enhanced ACA application as part of the fixed, bundled price charged per billing period. On January 20, 2017, President Donald J. Trump issued an executive order stating that it is the policy of the new administration to seek the prompt repeal of the ACA. Despite multiple efforts, Congress was unable to pass legislation significantly repealing or replacing the ACA in 2017, but many uncertainties remain regarding its future. The Trump Administration took additional action in October 2017 that may weaken the ACA’s public health insurance marketplace, and the Tax Cuts and Jobs Act of 2017, enacted December 22, 2017, eliminates the ACA’s individual mandate penalty beginning January 1, 2019. Both events suggest additional action to further weaken, repeal or replace the ACA may occur. The modification or repeal of certain provisions of the ACA could harm our business, operating results and financial condition. If the ACA is modified to eliminate the employer reporting requirements, or if the ACA is repealed and replaced with new legislation that does not include similar employer reporting requirements, we will no longer generate revenues in connection with processing and filing Forms 1094 and 1095 on behalf of clients. While we generally do not track our revenues on an application-by-application basis (because applications are often sold in various groupings and configurations for a single price), we estimate that, if the ACA is not modified or repealed, revenues from our Enhanced ACA application and ACA forms filings business will represent approximately 4% of total projected revenues for the year ending December 31, 2019. Further, uncertainty regarding the potential future modification, repeal or replacement of the ACA could adversely affect our ability to sell our Enhanced ACA application to new clients.

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

Our success is dependent in part upon our intellectual property. We rely on a combination of copyrights, trademarks, service marks, trade secret laws and contractual restrictions to establish and to protect our intellectual property rights. However, the steps we take to protect our intellectual property may be inadequate. We will not be able to protect our intellectual property if we are unable to enforce our rights or if we do not detect unauthorized use of our intellectual property. Despite our precautions, it may be possible for unauthorized third parties to copy our applications and use information that we regard as proprietary to create products or services that compete with ours.

We may be required to spend significant resources to monitor and protect our intellectual property. We have been involved in litigation in the past and litigation may be necessary in the future to protect and enforce our intellectual property rights and to protect our trade secrets. Such litigation could be costly, time-consuming and distracting to management and could result in the impairment or loss of portions of our intellectual property. Furthermore, our efforts to enforce our intellectual property rights may be met with defenses, counterclaims and countersuits attacking the validity and enforceability of our intellectual property rights. We may not be able to secure, protect and enforce our intellectual property rights or control access to, and the distribution of, our solution and proprietary information, which could adversely affect our business.

We may be sued by third parties for alleged infringement of their proprietary rights.

Considerable intellectual property development activity exists in our industry, and we expect that software developers will increasingly be subject to infringement claims as the number of applications and competitors grows and the functionality of applications in different industry segments overlaps. Our competitors, as well as a number of other entities and individuals, may own or claim to own intellectual property in technology areas relating to our solution or applications. In addition, we may increasingly be subject to trademark infringement claims as our presence grows in the marketplace. From time to time, third parties have asserted and may in the future assert that we are infringing on their intellectual property rights, and we may be found to be infringing upon such rights. A claim of infringement may also be made relating to technology that we acquire or license from third parties. However, we may be unaware of the intellectual property rights of others that may cover, or may be alleged to cover, some or all of our solution, applications or brands.

The outcome of litigation is inherently unpredictable and, as a result, any future litigation or claim of infringement could (i) cause us to enter into an unfavorable royalty or license agreement, pay ongoing royalties or require that we comply with other unfavorable terms, (ii) require us to discontinue the sale of our solution or applications, (iii) require us to indemnify our clients or third-party service providers or (iv) require us to expend additional development resources to redesign our solution or applications. Any of these outcomes could harm our business. Even if we were to prevail, any litigation regarding our intellectual property could be costly and time consuming and divert the attention of our management and key personnel from our business and operations.

The use of open source software in our applications may expose us to additional risks and harm our intellectual property rights.

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

We employ third-party licensed software for use in our applications and the inability to maintain these licenses or errors in the software we license could result in increased costs or reduced service levels, which could adversely affect our business.

Our applications incorporate certain third-party software obtained under licenses from other companies. We anticipate that we will continue to rely on such third-party software and development tools from third parties in the future. Although we believe that there are commercially reasonable alternatives to the third-party software we currently license, this may not always be the case, or it may be difficult or costly to replace. In addition, incorporating the software used in our applications with new third-party software may require significant work and substantial investment of our time and resources. Also, to the extent that our applications depend upon the successful operation of third-party software in conjunction with our software, any undetected errors or defects in this third-party software could prevent the deployment or impair the functionality of our applications, delay new application introductions, result in a failure of our applications and harm our reputation.

Adverse economic and market conditions could affect our business, operating results or financial condition.

Our business depends on the overall demand for HCM applications and on the economic health of our current and prospective clients. If economic conditions in the United States or in global markets deteriorate, clients may cease their operations, eliminate or reduce unscheduled payroll runs (such as bonuses), reduce headcount, delay or reduce their spending on HCM and other outsourcing services or attempt to renegotiate their contracts with us. An economic decline could result in reductions in sales of our applications, decreased revenue from unscheduled payroll runs and fees charged on a per-employee basis, longer sales cycles, slower adoption of new technologies and increased price competition, any of which could adversely affect our business, operating results or financial condition. In addition, HCM spending levels may not increase following any recovery.

In recent years, there have been several instances when there has been uncertainty regarding the ability of Congress and the President collectively to reach agreement on federal budgetary and spending matters. A period of failure to reach agreement on these matters, particularly if accompanied by an actual or threatened government shutdown, may have an adverse impact on the U.S. economy. Additionally, because certain of our clients rely on government resources to fund their operations, a prolonged government shutdown may affect such clients' ability to make timely payments to us, which could adversely affect our operations results or financial condition.

Further, as part of our payroll and tax filing application, we collect and then remit client funds to taxing authorities and accounts designated by our clients. During the interval between receipt and disbursement, we may invest such funds in money market funds, demand deposit accounts, certificates of deposit and commercial paper. These investments are subject to general market, interest rate, credit and liquidity risks, and such risks may be exacerbated during periods of unusual financial market volatility. Any loss of or inability to access such funds could have an adverse impact on our cash position and results of operations and could require us to obtain additional sources of liquidity, which may not be available on terms that are acceptable to us, if at all.

Our outstanding indebtedness is subject to certain operating and financial covenants that may restrict our business and financing activities and may adversely affect our cash flow and our ability to operate our business.

We have incurred indebtedness to fund certain construction projects at our corporate headquarters. Pursuant to the terms of our outstanding indebtedness, we may not, subject to certain exceptions:

- incur additional debt;
- create or permit the existence of additional liens on our assets;
- permit certain fundamental changes, including a merger with any persons;
- make investments in and acquisitions of (or acquisitions of substantially all of the assets of) any person;
- enter into transactions with affiliates other than in the ordinary course of business on an arm's-length basis;
- make any distributions during an event of default, or any other distributions in excess of $50 million prior to demonstrating pro forma compliance with certain financial covenants;

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- make any change in the basis upon which our financial statements are prepared;
- enter into any sale and leaseback transaction; or
- amend, modify, or waive any of our organizational documents in a manner that would be adverse to our lenders.

In addition, we are required to maintain a fixed charge coverage ratio of earnings before interest, taxes, depreciation and amortization ("EBITDA") to fixed charges (defined as current maturities of long-term debt, interest expense, rent expense and distributions) of not less than 1.25 to 1.0 and a funded indebtedness (defined as total indebtedness less accounts payable, accrued expenses and deferred revenues) to EBITDA of not greater than 2.0 to 1.0. The operating and financial covenants in the loan agreements relating to our outstanding indebtedness, as well as any future financing agreements that we may enter into, may restrict our ability to finance our operations, engage in business activities or expand or fully pursue our business strategies. We may also be required to use a substantial portion of our cash flows to pay principal and interest on our debt, which would reduce the amount of money available for operations, working capital, expansion, or other general corporate purposes.

Our ability to meet our expenses and debt obligations and comply with the operating and financial covenants may be affected by financial, business, economic, regulatory and other factors beyond our control. We may be unable to control many of these factors and comply with these covenants. A breach of any of the covenants under our loan agreements could result in an event of default, which could cause all of our outstanding indebtedness to become immediately due and payable.

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

In the future, we may seek to acquire or invest in businesses, applications or technologies that we believe complement or expand our applications, enhance our technical capabilities or otherwise offer growth opportunities. The pursuit of potential acquisitions may divert the attention of management and cause us to incur expenses in identifying, investigating and pursuing suitable acquisitions, whether or not they are ultimately consummated.

We do not have any experience in acquiring other businesses. If we acquire additional businesses, we may not be able to integrate the acquired personnel, operations and technologies successfully or to effectively manage the combined business following the acquisition. We also may not achieve the anticipated benefits from the acquired business due to a number of factors, including:

- the inability to integrate or benefit from acquired applications or services in a profitable manner;
- unanticipated costs or liabilities associated with the acquisition;
- the incurrence of acquisition-related costs;
- difficulty integrating the accounting systems, operations and personnel of the acquired business;
- difficulty and additional expenses associated with supporting legacy products and hosting infrastructure of the acquired business;
- difficulty converting the clients of the acquired business onto our solution, including disparities in the revenues, licensing, support or services of the acquired company;
- diversion of management's attention from other business concerns;
- harm to our existing relationships with clients as a result of the acquisition;
- the potential loss of key employees;
- the use of resources that are needed in other parts of our business; and
- the use of substantial portions of our available cash to consummate the acquisition.

In addition, a significant portion of the purchase price of any companies we acquire may be allocated to acquired goodwill and other intangible assets, which must be assessed for impairment at least annually. In the future, if our acquisitions do not yield expected returns, we may be required to take charges to our operating results based on this impairment assessment process, which could harm our results of operations. Acquisitions could also result in issuances of equity securities or the incurrence of debt, which would result in dilution to our stockholders.

Our growth depends in part on the success of our relationships with third parties.

We rely on third-party financial and accounting processing systems, as well as various financial institutions, to perform financial services in connection with our applications, such as providing automated clearing house ("ACH") and wire transfers as part of our payroll and expense reimbursement services and to provide technology and content support, manufacture time clocks and process background checks. We anticipate that we will continue to depend on various third-party relationships in order to grow our business, provide technology and content support, manufacture time clocks and process background checks. Identifying, negotiating and documenting relationships with these third parties and integrating third-party content and technology requires significant time and resources. Our agreements with third parties typically are non-exclusive and do not prohibit them from working with our competitors. In addition, these third parties may not perform as expected under our agreements, and we may have disagreements or disputes with such third parties, which could negatively affect our brand and reputation. A global economic slowdown could also adversely affect the businesses of our third-party providers, particularly those financial institutions that process transactions through the ACH network, and it is possible that they may not be able to devote the resources we expect to our relationship.

If we are unsuccessful in establishing or maintaining our relationships with these third parties, our ability to compete in the marketplace or to grow our revenues could be impaired and our business, operating results or financial condition could be adversely affected. Even if we are successful, these relationships may not result in improved operating results.

If our goodwill or other intangible assets become impaired, we may be required to record a significant charge to earnings.

We are required to test goodwill for impairment at least annually or earlier if events or changes in circumstances indicate the carrying value may not be recoverable. As of December 31, 2018, we had recorded a total of $51.9 million of goodwill and $0.7 million of other intangible assets. An adverse change in domestic or global market conditions, particularly if such change has the effect of changing one of our critical assumptions or estimates made in connection with the impairment testing of goodwill or intangible assets, could result in a change to the estimation of fair value that could result in an impairment charge to our goodwill or other intangible assets. Any such material charges may have a negative impact on our operating results or financial condition.

We may pay employees and taxing authorities amounts due for a payroll period before a client’s electronic funds transfers are finally settled to our account. If client payments are rejected by banking institutions or otherwise fail to clear into our accounts, we may require additional sources of short-term liquidity and our operating results could be adversely affected.

Our payroll processing application moves significant funds from the account of a client to employees and relevant taxing authorities. For larger funding amounts, we require clients to transfer the funds to us via fed wire. For smaller funding amounts, we debit a client’s account prior to any disbursement on its behalf, and due to ACH banking regulations, funds previously credited could be reversed under certain circumstances and time frames after our payment of amounts due to employees and taxing and other regulatory authorities. There is therefore a risk that the employer’s funds will be insufficient to cover the amounts we have already paid on its behalf. While such shortage and accompanying financial exposure has only occurred in very limited circumstances in the past, should clients default on their payment obligations in the future, we might be required to advance substantial funds to cover such obligations. In such an event, we may be required to seek additional sources of short-term liquidity, which may not be available on reasonable terms, if at all, and our operating results and our liquidity could be adversely affected and our banking relationships could be harmed.

Because our long-term success may depend, in part, on our ability to expand the sales of our solution to clients located outside of the United States, our business could be subject to risks associated with international operations.

An element of our growth strategy is to expand our operations and client base. To date, we have not engaged in any operations outside of the United States. If we decide to expand our operations into international markets, it will require significant resources and management attention and will subject us to regulatory, economic and political risks that are different from those in the United States. Because of our lack of experience with international operations, we cannot ensure that our international expansion efforts will be successful, and the impact of such expansion efforts may adversely affect our business, operating results or financial condition.

If we are unable to maintain effective internal control over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock may be negatively affected.

As a public company, we are required to maintain internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements. Management must evaluate and furnish a report on the effectiveness of our internal control over financial reporting as of the end of each fiscal year, and our auditors must attest to the effectiveness of our internal control over financial reporting.

If we have a material weakness in our internal control over financial reporting, we may not detect errors on a timely basis and our financial statements may be materially misstated. If we identify material weaknesses in our internal control over financial reporting or if our independent registered public accounting firm is unable to express an opinion as to the effectiveness of our internal control over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports and/or we could become subject to investigations by the New York Stock Exchange (the “NYSE”), the SEC, or other regulatory authorities and the market price of our common stock could be negatively affected.

Adverse tax laws or regulations could be enacted or existing laws could be applied to us or our clients, which could increase the costs of our solution and applications and could adversely affect our business, operating results or financial condition.

As a vendor of services, we are ordinarily held responsible by taxing authorities for collecting and paying any applicable sales or other similar taxes. Additionally, the application of federal, state and local tax laws to services provided electronically like ours is evolving. New income, sales, use or other tax laws, statutes, rules, regulations or ordinances could be enacted at any time (possibly with retroactive effect), and could be applied solely or disproportionately to services and applications provided over the internet. These enactments could adversely affect our sales activity, due to the inherent cost increase the taxes would represent, and ultimately could adversely affect our business, operating results or financial condition.

Each state has different rules and regulations governing sales and use taxes, and these rules and regulations are subject to varying interpretations that change over time. We review these rules and regulations periodically and, when we believe we are subject to sales and use taxes in a particular state, we may voluntarily engage state tax authorities in order to determine how to comply with that state’s rules and regulations. We cannot ensure that we will not be subject to sales and use taxes or related penalties for past sales in states where we currently believe no such taxes are required.

In addition, existing tax laws, statutes, rules, regulations or ordinances could be interpreted, changed, modified or applied adversely to us (possibly with retroactive effect), which could require us or our clients to pay additional tax amounts, as well as require us or our clients to pay fines or penalties and substantial interest for past amounts.   If we are unsuccessful in collecting such taxes from our clients, we could be held liable for such costs, thereby adversely affecting our business, operating results or financial condition. Additionally, the imposition of such taxes on us would effectively increase the cost of our software and services we provide to clients and would likely have a negative impact on our ability to retain existing clients or to gain new clients in the jurisdictions in which such taxes are imposed.

Our actual operating results may differ significantly from our guidance.

From time to time, we have released, and may continue to release, guidance in our earnings conference calls, earnings releases, or otherwise, regarding our future performance, which represents our estimates as of the date of release. This guidance, which includes forward-looking statements, has been and will be based on projections prepared by our management. These projections are not prepared with a view toward compliance with published guidelines of the American Institute of Certified Public Accountants, and neither our registered public accountants nor any other independent expert or outside party compiles or examines the projections. Accordingly, no such person expresses any opinion or any other form of assurance with respect to the projections.

Projections are based upon a number of assumptions and estimates that, while presented with numerical specificity, are inherently subject to significant business, economic, and competitive uncertainties and contingencies, many of which are beyond our control. Projections are also based upon specific assumptions with respect to future business decisions, some of which will change. The principal reason that we release guidance is to provide a basis for our management to discuss our business outlook with analysts and investors. We do not accept any responsibility for any projections or reports published by any third parties.

Guidance is necessarily speculative in nature, and it can be expected that some or all of the assumptions underlying the guidance furnished by us will vary significantly from actual results. Accordingly, our guidance is only an estimate of what management believes is realizable as of the date of release. Actual results may vary from our guidance and the variations may be material. In light of the foregoing, investors are urged not to rely upon our guidance in making an investment decision regarding our common stock.

Any failure to successfully implement our operating strategy or the occurrence of any of the events or circumstances set forth in this “Risk Factors” section in this Form 10-K could result in the actual operating results being different from our guidance, and the differences may be adverse and material.

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

Our certificate of incorporation authorizes us to issue up to one hundred million shares of common stock and up to ten million shares of preferred stock with such rights and preferences as may be determined by our board of directors. Subject to compliance with applicable rules and regulations, we may issue all of these shares that are not already outstanding without any action or approval by our stockholders. We intend to continue to evaluate strategic acquisitions in the future. We may pay for such acquisitions, in part or in full, through the issuance of additional equity securities.

Any issuance of shares in connection with an acquisition, the exercise of stock options or warrants, the award of shares of restricted stock or otherwise would dilute the percentage ownership held by our existing stockholders.

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

Our certificate of incorporation, bylaws and Delaware law contain provisions that may have the effect of delaying or preventing a change in control of us or changes in our management. These provisions, alone or together, could delay or prevent hostile takeovers and changes in control or changes in our management.

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

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.

Our certificate of incorporation contains an exclusive forum provision that may discourage lawsuits against us and our directors and officers.

Our certificate of incorporation provides that, unless we consent in writing to the selection of an alternative forum, the Court of Chancery of the State of Delaware (or if no Court of Chancery located within the State of Delaware has jurisdiction, the Federal District Court for the District of Delaware) will be the sole and exclusive forum any derivative action or proceeding brought on our behalf, any action asserting a claim of breach of fiduciary duty owed by any of our directors, officers or other employees to us or our stockholders, any action asserting a claim against us or any of our directors, officers or other employees arising pursuant to any provision of Delaware law or our certificate of incorporation or our bylaws (as either may be amended from time to time) or any action asserting a claim against us or any of our directors, officers or other employees governed by the internal affairs doctrine. This exclusive forum provision may limit the ability of our stockholders to bring a claim in a judicial forum that such stockholders find favorable for disputes with us or our directors or officers, which may discourage such lawsuits against us and our directors and officers. Alternatively, if a court outside of Delaware were to find this exclusive forum provision inapplicable to, or unenforceable in respect of, one or more of the specified types of actions or proceedings described above, we may incur additional costs associated with resolving such matters in multiple jurisdictions, which could materially and adversely affect our financial results.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

Our corporate headquarters is an approximately 500,000-square-foot campus located on over 30 acres of Company-owned property in Oklahoma City, Oklahoma. In addition to housing two fully redundant data centers at our corporate headquarters, we operate another fully redundant data center at a leased property near Dallas, Texas. In November 2018, we purchased approximately 14 acres of property in Grapevine, Texas, where we plan to build a new, expanded facility for our Texas operations. We also lease a disaster recovery site in downtown Oklahoma City.

We also lease offices in Arizona, California, Colorado, Connecticut, Florida, Georgia, Illinois, Indiana, Maryland, Massachusetts, Michigan, Minnesota, Missouri, New Jersey, New York, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Tennessee, Texas, Utah, Virginia, Washington and Wisconsin. We believe that these facilities are suitable for our current operations and upon the expiration of the terms of the leases we believe we could renew these leases or find suitable space elsewhere on acceptable terms.

Item 3. Legal Proceedings

From time to time, we are involved in various disputes, claims, suits, investigations and legal proceedings arising in the ordinary course of business. We believe that the resolution of current pending legal matters will not have a material adverse effect on our business, financial condition, results of operations or cash flows. Nonetheless, we cannot predict the outcome of these proceedings, as legal matters are subject to inherent uncertainties, and there exists the possibility that the ultimate resolution of these matters could have a material adverse effect on our business, financial condition, results of operations or cash flows.

Item 4. Mine Safety Disclosures

None.

PART II

Item 5. Market for Registrants Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is traded on the NYSE under the symbol “PAYC.” As of February 5, 2019, there were approximately 1,142 holders of record of our common stock. This number is based on the actual number of holders registered at such date and does not include holders whose shares are held in “street name” by brokers and other nominees.

Dividends

We did not pay any cash dividends on our common stock in 2018, 2017 or 2016. The declaration, amount and payment of any future dividends on shares of common stock will be at the sole discretion of our board of directors and we may reduce or discontinue entirely the payment of such dividends at any time. Our board of directors may take into account general and economic conditions, our financial condition and operating results, our available cash and current and anticipated cash needs, capital requirements, contractual, legal, tax and regulatory restrictions and implications of the payment of dividends by us to our stockholders or by our subsidiaries to us, and such other factors as our board of directors may deem relevant. While there are no restrictions that currently apply under our existing loan agreements, such agreements prohibit the payment of dividends if an event of default exists. In addition, any financing arrangements that we enter into in the future may include restrictive covenants that limit our or our subsidiaries’ ability to pay dividends.

We are a holding company that has no material assets other than our ownership of all of the outstanding Series B Preferred Units of Paycom Payroll Holdings, LLC (“Holdings”) and the outstanding capital stock of WCAS Paycom Holdings, Inc. and WCAS CP IV Blocker, Inc. In the event that we decide to pay dividends in the future, we intend to cause Holdings to make distributions to us in an amount sufficient to cover cash dividends, if any, declared by us.

Performance Graph

Notwithstanding any statement to the contrary in any of our filings with the SEC, the following performance graph shall not be deemed “filed” with the SEC for purposes of Section 18 of the Exchange Act or “soliciting material” under the Exchange Act and shall not be incorporated by reference into any such filings irrespective of any general incorporation language contained in such filing.

The following graph compares the cumulative total stockholder return on our common stock with the cumulative total return of the S&P 500 Index and the S&P 1500 Application Software Index during the period commencing on April 15, 2014, the initial trading day of our common stock, and ending on December 31, 2018. The graph assumes that $100 was invested at the beginning of the period in our common stock and in each of the comparative indices, and assumes the reinvestment of any dividends. Historical stock price performance should not be relied upon as an indication of future stock price performance.

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Purchases of Equity Securities

The number of shares of common stock repurchased by us during the three months ended December 31, 2018 is set forth below:

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (1)
October 1 - 31, 2018	65,528	$ 121.93	65,528	$ 66,400,000
November 1 - 30, 2018(2)	436,199	$ 124.88	436,199	$ 162,000,000
December 1 - 31, 2018	—	$ —	—	$ 162,000,000
Total	501,727		501,727	

(1) Under a stock repurchase plan announced on October 31, 2017, we were authorized to purchase (in the aggregate) up to $75.0 million of our common stock. We announced on February 13, 2018 that the stock repurchase plan was amended to add $100.0 million of availability and extend the expiration date to February 12, 2020. On November 20, 2018, we announced that our Board of Directors authorized a new stock repurchase plan, pursuant to which we are authorized to purchase (in the aggregate) up to $150.0 million of our common stock in open market purchases, privately negotiated transactions or by other means. The current stock repurchase plan expires on November 19, 2020.

(2) Includes 1,049 shares withheld to satisfy tax withholding obligations for certain employees upon the vesting of restricted stock.

Item 6.Selected Financial Data

Our selected consolidated financial data set forth below should be read together with Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes thereto, which are included elsewhere in this Form 10-K. The selected consolidated financial data for the years ended December 31, 2018, 2017 and 2016 reflects the adoption of Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers ("Topic 606"). See Note 2 in the notes to our consolidated financial statements for a summary of adjustments as a result of the adoption of Topic 606 for the years ended December 31, 2017 and 2016. The selected financial data for the years ended December 31, 2015 and 2014 has not been adjusted to reflect the adoption of Topic 606.

	Year Ended December 31,				
	2018	2017 *As Adjusted	2016 *As Adjusted	2015	2014
	(dollars in thousands, except share and per share data)				
Consolidated statements of income data:					
Total revenues	$566,336	$433,047	$329,141	$224,653	$150,929
Operating income	$173,715	$129,710	$101,740	$34,435	$15,700
Net income	$137,065	$123,486	$70,421	$20,945	$5,663
Earnings per share, basic	$2.37	$2.13	$1.21	$0.37	$0.11
Earnings per share, diluted	$2.34	$2.10	$1.19	$0.36	$0.11
Weighted average shares outstanding:					
Basic	57,711,315	57,839,155	57,550,204	56,495,170	49,784,154
Diluted	58,582,486	58,790,019	58,968,099	57,919,700	51,857,309

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 in the notes to our consolidated financial statements for a description of adjustments.

	As of December 31,				
	2018	2017 *As Adjusted	2016 *As Adjusted	2015	2014
	(in thousands)				
Consolidated balance sheets data:					
Cash and cash equivalents	$45,718	$46,077	$60,158	$50,714	$25,144

Working capital[1]	$44,920	$43,095	$51,167	$37,330	$15,340
Property and equipment, net	$176,962	$147,705	$96,848	$58,858	$47,919
Total assets	$1,521,926	$1,550,138	$1,224,589	$876,655	$797,497
Deferred revenue	$64,651	$51,624	$39,711	$29,036	$19,337
Net long-term debt, less current portion	$32,614	$34,414	$28,711	$24,856	$26,123
Additional paid in capital	$203,680	$161,809	$120,027	$71,135	$67,937
Retained earnings	$395,590	$258,525	$135,040	$26,608	$5,663
Total stockholder's equity	$334,753	$281,247	$205,694	$98,314	$74,138

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 in the notes to our consolidated financial statements for a description of adjustments.

(1) Working capital is defined as current assets, excluding restricted cash, less current liabilities, excluding the current portion of deferred revenue.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with the audited and unaudited consolidated financial statements (prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP")) and related notes included elsewhere in this Annual Report on Form 10-K (this "Form 10-K"). The following discussion contains forward-looking statements that are subject to risks and uncertainties. See Part I "Special Note Regarding Forward-Looking Statements" for a discussion of the uncertainties, risks, and assumptions associated with those statements. Actual results could differ materially from those discussed in or implied by forward- looking statements as a result of various factors, including those discussed below and elsewhere in this Form 10-K, particularly in the section entitled "Risk Factors." Unless we state otherwise or the context otherwise requires, the terms "we," "us," "our" and the "Company" refer to Paycom Software, Inc. and its consolidated subsidiaries.

Overview

We are a leading provider of comprehensive, cloud-based human capital management ("HCM") software delivered as Software-as-a-Service. We provide functionality and data analytics that businesses need to manage the complete employment lifecycle, from recruitment to retirement. Our solution requires virtually no customization and is based on a core system of record maintained in a single database for all HCM functions, including talent acquisition, time and labor management, payroll, talent management and human resources management applications. Our user-friendly software allows for easy adoption of our solution by employees, enabling self-management of their HCM activities in the cloud, which reduces the administrative burden on employers and increases employee productivity.

We generate revenues from (i) fixed amounts charged per billing period plus a fee per employee or transaction processed and (ii) fixed amounts charged per billing period. We do not require clients to enter into long-term contractual commitments with us. Our billing period varies by client based on when they pay their employees, which is either weekly, bi-weekly, semi-monthly or monthly. Our revenues are primarily generated through our sales force that solicits new clients and our client relations representatives who sell new applications to existing clients.

We serve a diverse client base in terms of size and industry. None of our clients constituted more than one-half of one percent of our revenues for the year ended December 31, 2018. We stored data for over 4.1 million persons employed by our clients during the year ended December 31, 2018.

Our continued growth depends on the introduction of new applications to our existing client base while targeting a high degree of client employee usage across those applications, attracting new clients through further penetration of our existing markets and geographic expansion into new markets. During the year ended December 31, 2018, we opened new sales offices in Salt Lake City, Utah, Rochester, New York, Columbus, Ohio and San Diego, California. The opening of these four new sales offices brings our total number of sales teams to 49 sales teams located in 26 states. We plan to open additional sales offices in the future to further expand our presence in the U.S. market. We also plan to relocate our Texas operations to a new, expanded facility in Grapevine, Texas, with construction scheduled to begin in the first half of 2019. Our principal marketing efforts include email campaigns, social and digital media, search engine marketing methods, tradeshows and outbound marketing including television and print advertising. In addition, we generate leads and build recognition of our brand and thought leadership with relevant and informative content, such as white papers, blogs, podcast episodes and webinars.

During the last three years, we have developed several new applications. We believe our ability to continue to develop new applications and to improve existing applications will enable us to increase revenues in the future, and the number of our new applications adopted by our clients has been a significant factor in our revenue growth over the last three years.

Growth Outlook, Opportunities and Challenges

Based on our total revenues, we have grown at a 39% compound annual growth rate from January 1, 2015 through December 31, 2018. As a result of our significant revenue growth and geographic expansion since our initial public offering in April 2014, we are presented with a variety of opportunities and challenges. Our payroll application is the foundation of our solution, and all of our clients are required to utilize this application in order to access our other applications. Consequently, we have historically generated the majority of our revenues from our payroll applications, although our revenue mix has evolved and will continue to evolve as we develop and add new non-payroll applications to our solution. We believe our strategy of focusing on increased employee usage is key to long-term client satisfaction and client retention. Client adoption of new applications and client employee usage of both new and existing applications have been significant factors in our revenue growth, and we expect the continuation of this trajectory will depend, in part, on the introduction of applications to our existing client base that encourage and promote more employee usage. Moreover, in order to increase revenues and continue to improve our operating results, we must also attract new clients. We intend to obtain new clients by (i) continuing to leverage our salesforce productivity within markets where we currently have existing sales offices, (ii) expanding our presence in metropolitan areas where we currently have an existing sales office through adding sales teams or offices, thereby increasing the number of sales professionals within such markets, and (iii) opening sales offices in new metropolitan areas.

Our target client size range is 50 to 5,000 employees. While we continue to serve a diversified client base ranging in size from one employee to many thousands of employees, the average size of our clients has grown significantly as we have organically grown our operations, increased the number of applications we offer and experienced traction with larger companies. Our solution requires no adjustment to serve larger clients. We believe larger employers represent a substantial opportunity to increase the number of potential clients and to increase our revenues per client, with limited incremental cost to us. Because we charge our clients on a per-employee basis for certain services we provide, any increase or decrease in the number of employees at our clients will have a positive or negative impact, respectively, on our results of operations. We expect that changes in certain factors affecting our performance will correlate with improvement or deterioration in the labor market.

Throughout our history, we have built strong relationships with our clients. As the HCM needs of our clients evolve, we believe that we are well-positioned to gain additional share of the HCM spending of our clients, and we believe this opportunity is significant. To be successful, we must continue to demonstrate the operational and economic benefits of our solution, as well as effectively hire, train, motivate and retain qualified personnel.

Growing our business has resulted in, and will continue to result in, substantial investments in sales professionals, operating expenses, system development and programming costs and general and administrative expenses, which have and will continue to increase our expenses. Specifically, our revenue growth and geographic expansion drive increases in our employee headcount, which in turn precipitates an increase in (i) salaries and benefits, (ii) stock-based compensation expense and (iii) facility costs related to the expansion of our corporate headquarters, operations facilities and additional sales office leases.

We believe the challenges of managing the ever-changing complexity of payroll and human resources will continue to drive companies to turn to outsourced providers for help with their HCM needs. The HCM industry historically has been driven, in part, by legislation and regulatory action, including COBRA, changes to the minimum wage laws or overtime rules, and legislation from federal, state or municipal taxation authorities. The implementation of the Affordable Care Act (the “ACA”) is an example of legislation that has created demand in the HCM industry. We generate ACA-related revenues (i) on an annual basis in connection with processing and filing Forms 1094 and 1095 on behalf of clients and (ii) from clients who have purchased our Enhanced ACA application as part of the fixed, bundled price charged per billing period. While we generally do not track our revenues on an application-by-application basis (because applications are often sold in various groupings and configurations for a single price), we estimate that, if the ACA is not modified or repealed, revenues from our Enhanced ACA application and ACA forms filings business will represent approximately 4% of total projected revenues for the year ending December 31, 2019.

For the years ended December 31, 2018, 2017 and 2016, our gross margins were approximately 84%, 83% and 84%, respectively. Although our gross margins may fluctuate from quarter to quarter due to seasonality and hiring trends, we expect our gross margins will remain relatively constant in future periods.

Key Metrics

In addition to the U.S. GAAP and non-GAAP metrics discussed elsewhere in this Form 10-K, we also monitor the following metrics to evaluate our business, measure our performance and identify trends affecting our business:

	Year Ended December 31,		
	2018	2017	2016
Key performance indicators:			
Clients	23,533	20,591	17,817
Clients (based on parent company grouping)	12,754	11,111	10,464
Sales teams	49	45	42
Annual revenue retention rate	92 %	91 %	91 %

- Clients. When we calculate the number of clients at period end, we treat client accounts with separate taxpayer identification numbers as separate clients, which often separates client accounts that are affiliated with the same parent organization. We track the number of our clients to provide an accurate gauge of the size of our business. Unless we state otherwise or the context otherwise requires, references to clients throughout this Form 10-K refer to this metric.
- Clients (based on parent company grouping). When we calculate the number of clients based on parent company grouping at period end, we combine client accounts that have identified the same person(s) as their decision-maker regardless of whether the client accounts have separate taxpayer identification numbers, which often combines client accounts that are affiliated with the same parent organization. We track the number of our clients based on parent company grouping to provide an alternate measure of the size of our business and clients.

- Sales Teams. We monitor our sales professionals by the number of sales teams at period end. Each team consists of a sales manager and approximately six to eight sales professionals. Certain larger metropolitan areas can support more than one sales team. We believe the number of sales teams is an indicator of potential revenues for future periods.
- Annual Revenue Retention Rate. Our annual revenue retention rate tracks the percentage of revenues that we retain from our existing clients. We monitor this metric because it is an indicator of client satisfaction and revenues for future periods.

Components of Results of Operations

Sources of Revenues

Revenues are comprised of recurring revenues, and implementation and other revenues. We expect our revenues to increase as we introduce new applications, expand our client base and renew and expand relationships with existing clients. As a percentage of total revenues, we expect our mix of recurring revenues, and implementation and other revenues to remain relatively constant.

Recurring Revenues

Recurring revenues include fees for our talent acquisition, time and labor management, payroll, talent management and HR management applications as well as fees charged for form filings and delivery of client payroll checks and reports. These revenues are derived from (i) fixed amounts charged per billing period plus a fee per employee or transaction processed or (ii) fixed amounts charged per billing period. We do not require clients to enter into long-term contractual commitments with us. Our billing period varies by client based on when they pay their employees, which is done either weekly, bi-weekly, semi-monthly or monthly. Because recurring revenues are based, in part, on fees for use of our applications and the delivery of checks and reports that are levied on a per-employee basis, our recurring revenues increase as our clients hire more employees. Recurring revenues are recognized in the period services are rendered.

Recurring revenues include revenues relating to the annual processing of payroll forms, such as Form W-2 and Form 1099, and revenues from processing unscheduled payroll runs (such as bonuses) for our clients. Because payroll forms are typically processed in the first quarter of the year and many of our clients have been subject to ACA form filing requirements in the first quarter, first quarter revenues and margins are generally higher than in subsequent quarters. We anticipate our revenues will continue to exhibit this seasonal pattern related to ACA form filings for so long as the ACA (or replacement legislation) includes employer reporting requirements. In addition, we often experience increased revenues during the fourth quarter due to unscheduled payroll runs for our clients that occur before the end of the year. Therefore, we expect the seasonality of our revenue cycle to decrease to the extent clients utilize more of our non-payroll applications.

Beginning April 1, 2016, recurring revenues also include interest earned on funds held for clients. We collect funds from clients in advance of either the applicable due date for payroll tax submissions or the applicable disbursement date for employee payment services. These collections from clients are typically disbursed from one to 30 days after receipt, with some funds being held for up to 120 days. We typically invest funds held for clients in money market funds, demand deposit accounts, commercial paper and certificates of deposit until they are paid to the applicable tax or regulatory agencies or to client employees. We expect interest earned on funds held for clients will increase as we introduce new applications, expand our client base and renew and expand relationships with existing clients. The amount of interest we earn from the investment of client funds is also impacted by changes in interest rates.

Implementation and Other Revenues

Implementation and other revenues are comprised of implementation fees for the deployment of our solution and other revenues from sales of time clocks as part of our time and attendance services. Non-refundable implementation fees are charged to new clients at inception and upon the addition of certain incremental applications for existing clients. These fees range from 10% to 30% of the annualized value of the transaction. Implementation revenues are recognized as deferred revenue and amortized into income over the life of the client, which is estimated to be ten years, and other revenues are recognized upon shipment of time clocks. Implementation and other revenues comprised approximately 1.6% and 1.8% of our total revenues for the years ended December 31, 2018 and 2017, respectively.

Cost of Revenues

Cost of revenues consists of expenses related to hosting and supporting our applications, hardware costs, systems support and technology and depreciation and amortization. These costs include employee-related expenses (including non-cash stock-based compensation expenses) and other expenses related to client support, bank charges for processing ACH transactions, certain implementation expenses, delivery charges and paper costs. They also include our cost for time clocks sold and ongoing technology and support costs related to our systems. The amount of depreciation and amortization of property and equipment allocated to cost of revenues is determined based upon an estimate of assets used to support our operations.

Administrative Expenses

Administrative expenses consist of sales and marketing, research and development, general and administrative and depreciation and amortization. Sales and marketing expenses consist primarily of employee-related expenses for our direct sales and marketing staff (such as the amortization of commissions and bonuses and non-cash stock-based compensation expenses), marketing expenses and other related costs. Research and development expenses consist primarily of employee-related expenses (including non-cash stock-based compensation expenses) for our development staff, net of capitalized software costs for internally developed software. We expect to grow our research and development efforts as we continue to broaden our payroll and HR solution offerings and extend our technological solutions by investing in the development of new applications. General and administrative expenses consist of employee-related expenses for finance and accounting, legal, human resources and management information systems personnel (including non-cash stock-based compensation expenses), legal costs, professional fees and other corporate expenses. Depreciation and amortization expenses consist of (i) the amount of depreciation and amortization of property and equipment allocated to administrative expenses (based upon an estimate of assets used to support our selling, general and administrative functions) and (ii) amortization of intangible assets.

Interest Expense

Interest expense includes interest on debt related to our corporate headquarters and settlements related to an interest rate swap we entered into in connection with such debt.

Other Income, net

Other income, net includes interest earned on our own funds, any gain or loss on the sale or disposal of fixed assets, costs associated with the early repayment of debt and any unrealized gain or loss related to our interest rate swap. Prior to April 1, 2016, other income, net also included interest earned on funds held for clients.

Provision for Income Taxes

Our consolidated financial statements include a provision for income taxes incurred for the anticipated tax consequences of the reported results of operations using the asset and liability method. Under this method, we recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial reporting and tax basis of assets and liabilities, as well as for any operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using the tax rates expected to apply to taxable income for the years in which those tax assets and liabilities are expected to be realized or settled. We recognize a valuation allowance to reduce deferred tax assets to the net amount we believe is more likely than not to be realized.

Results of Operations

The following table sets forth selected consolidated statements of income data and such data as a percentage of total revenues for each of the periods indicated, as well as year-over-year changes with respect to each line item:

	Year Ended December 31,							
	2018		2017 *As Adjusted		% change 2018 to 2017	2016 *As Adjusted		% change 2017 to 2016
	(dollars in thousands)							
Revenues								
Recurring	$557,255	98.4%	$425,424	98.2%	31%	$323,548	98.3%	31%
Implementation and other	9,081	1.6%	7,623	1.8%	19%	5,593	1.7%	36%
Total revenues	566,336	100.0%	433,047	100.0%	31%	329,141	100.0%	32%
Cost of revenues								
Operating expenses	76,231	13.5%	62,438	14.4%	22%	48,268	14.6%	29%
Depreciation and amortization	14,532	2.5%	9,590	2.2%	52%	5,798	1.8%	65%
Total cost of revenues	90,763	16.0%	72,028	16.6%	26%	54,066	16.4%	33%
Administrative expenses								
Sales and marketing	143,881	25.4%	110,846	25.6%	30%	85,361	25.9%	30%
Research and development	46,247	8.2%	30,430	7.0%	52%	20,966	6.4%	45%
General and administrative	96,605	17.1%	80,228	18.5%	20%	59,174	18.0%	36%
Depreciation and amortization	15,125	2.7%	9,805	2.3%	54%	7,834	2.4%	25%
Total administrative expenses	301,858	53.4%	231,309	53.4%	30%	173,335	52.7%	33%
Total operating expenses	392,621	69.4%	303,337	70.0%	29%	227,401	69.1%	33%
Operating income	173,715	30.6%	129,710	30.0%	34%	101,740	30.9%	27%
Interest expense	(766)	(0.1%)	(911)	(0.2%)	-16%	(1,036)	(0.3%)	(12%)
Other income, net	1,762	0.3%	(1,067)	(0.3%)	-265%	308	0.1%	(446%)
Income before income taxes	174,711	30.8%	127,732	29.5%	37%	101,012	30.7%	26%
Provision for income taxes	37,646	6.6%	4,246	1.0%	787%	30,591	9.3%	(86%)
Net income	$137,065	24.2%	$123,486	28.5%	11%	$70,421	21.4%	75%

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 in the notes to our consolidated financial statements for a description of adjustments.

Revenues

The increase in total revenues for the year ended December 31, 2018 from the year ended December 31, 2017 was primarily the result of (i) the addition of new clients and productivity and efficiency gains in mature sales offices, which are offices that have been open for at least 24 months, and in sales offices that reached maturity in 2018, (ii) contributions from new sales offices opened in 2017 that were progressing to maturity during 2018, (iii) the sale of additional applications to our existing clients, (iv) the strong performance of our tax forms filing business and (v) higher average interest rates earned on funds held for clients.

The increase in implementation and other revenues for the year ended December 31, 2018 from the year ended December 31, 2017 was primarily the result of the recognition of additional non-refundable conversion fees that are charged to new clients to offset the expense of new client set-up. These fees are deferred and recognized ratably over the ten-year estimated life of our clients.

The increase in total revenues for the year ended December 31, 2017 from the year ended December 31, 2016 was primarily the result of (i) the addition of new clients in mature sales offices, (ii) contributions from the six new sales offices opened in 2016 that were progressing to maturity during 2017, (iii) the sale of additional applications to our existing clients, (iv) the strong performance of our tax forms filing business and (v) growth in our clients' employee headcounts as a result of favorable economic conditions. Nonetheless, the magnitude of the increases in revenues for the year ended December 31, 2017 was offset, in part, due to the impact of hurricanes in Texas and Florida in August and September. In particular, we experienced some disruption to our prospecting and conversion efforts in the affected areas as well as implementation delays for new clients.

The increase in implementation and other revenues for the year ended December 31, 2017 from the year ended December 31, 2016 was primarily the result of the recognition of additional non-refundable conversion fees that are charged to new clients to offset the expense of new client set-up. These fees are deferred and recognized ratably over the ten-year estimated life of our clients.

Expenses

Cost of Revenues

The increase in cost of revenues of $18.7 million for the year ended December 31, 2018 from the year ended December 31, 2017 was primarily due to an $8.9 million increase in operating expenses attributable to growth in the number of operating personnel, a $4.7 million increase in shipping and automated clearing house fees related to the year-over-year increase in revenues and a $0.1 million increase in non-cash stock-based compensation expense. Depreciation and amortization expense increased $4.9 million, or 52%, primarily due to placing our fourth headquarters building in service in June 2018, the development of additional technology and purchases of other assets.

The increase in cost of revenues of $18.0 million for the year ended December 31, 2017 from the year ended December 31, 2016 was primarily due to a $12.2 million increase in employee-related expenses, which consisted of a $10.5 million increase in expenses attributable to growth in the number of operating personnel and a $1.7 million increase in non-cash stock-based compensation expense. Additionally, shipping fees and ACH fees increased $1.1 million and $0.9 million, respectively, in connection with increased sales. Depreciation and amortization expense increased $3.8 million, or 65%, primarily due to the development of additional technology and purchases of other assets, particularly with respect to the new headquarters building that was not in service for the entire prior year period.

Administrative Expenses

Sales and marketing

During the year ended December 31, 2018, sales and marketing expenses increased from the prior year by $33.0 million due to a $23.7 million increase in employee-related expenses, including commissions, bonuses and non-cash stock-based compensation, and a $9.3 million increase in marketing and advertising expense, primarily due to a national advertising campaign executed in the second half of 2018. The increase in employee-related expenses included a $2.5 million increase in non-cash stock-based compensation expense.

During the year ended December 31, 2017, sales and marketing expenses increased from the prior year by $25.5 million due to a $21.3 million increase in employee-related expenses, including commissions, bonuses and non-cash stock-based compensation, and a $4.2 million increase in marketing and advertising expense. The increase in employee-related expenses included a $2.0 million increase in non-cash stock-based compensation expense.

Research and development

During the year ended December 31, 2018, research and development expenses increased from the prior year due to a $15.8 million increase in employee-related expenses, including a $1.1 million increase in non-cash stock-based compensation expense.

During the year ended December 31, 2017, research and development expenses increased from the prior year due to a $9.5 million increase in employee-related expenses, including a $1.1 million increase in non-cash stock-based compensation expense.

As we continue to develop our platform and product offerings, we generally expect research and development expenses (exclusive of stock-based compensation) to continue to increase, particularly as we hire more personnel to support our growth. While we expect this trend to continue on an absolute dollar basis and as a percentage of total revenues, we also anticipate the rate of increase to decline over time as we leverage our growth and realize additional economies of scale.

Expenditures for software developed or obtained for internal use are capitalized and amortized over a three-year period on a straight-line basis. The nature of the development projects underway during a particular period directly impacts the timing and extent of these capitalized expenditures, and can affect the amount of research and development expenses in such period. The table below sets forth the amounts of capitalized and expensed research and development costs for the years ended December 31, 2018, 2017 and 2016:

	Year Ended December 31,			% Change	
	2018	2017	2016	2018 vs 2017	2017 vs 2016
	(in thousands)				
Capitalized portion of research and development	$22,013	$15,821	$8,817	39%	79%
Expensed portion of research and development	46,247	30,430	20,966	52%	45%
Total research and development costs	$68,260	$46,251	$29,783	48%	55%

General and administrative

During the year ended December 31, 2018, general and administrative expenses increased $16.4 million from the prior year due to an $18.4 million increase in employee-related expenses and a $1.3 million increase in accounting and legal expenses, partially offset by a $3.3 million decrease in non-cash stock-based compensation expense.

During the year ended December 31, 2017, general and administrative expenses increased $21.1 million from the prior year due to a $12.2 million increase in employee-related expenses and a $10.4 million increase in non-cash stock-based compensation expense, which were partially offset by a $1.5 million decrease in accounting and legal expenses.

Non-Cash Stock-Based Compensation Expense

	Year Ended December 31,			% Change	
	2018	2017 *As Adjusted	2016 *As Adjusted	2018 vs 2017	2017 vs 2016
	(in thousands)				
Non-cash stock-based compensation expense:					
Operating expenses	$4,041	$ 3,950	$ 2,217	2%	78%
Sales and marketing	7,510	5,023	3,028	50%	66%
Research and development	3,013	1,912	836	58%	129%
General and administrative	21,847	25,162	14,715	-13%	71%
Total non-cash stock-based compensation expense	$36,411	$ 36,047	$ 20,796	1%	73%

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 in the notes to our consolidated financial statements for a description of adjustments.

During the year ended December 31, 2018, our non-cash stock-based compensation expense increased $0.4 million from the prior year primarily due to the issuance and subsequent accelerated vesting of restricted stock subject to market-based vesting conditions during the first quarter of 2018, which exceeded expenses associated with the accelerated vesting of restricted stock subject to market-based vesting conditions in 2017.

During the year ended December 31, 2017, our non-cash stock-based compensation expense increased $15.3 million from the prior year primarily due to the vesting of restricted stock with market-based vesting conditions and the issuance of restricted stock with a higher grant-date fair value than shares issued in the prior year.

Depreciation and Amortization

During the years ended December 31, 2018 and 2017, depreciation and amortization expense increased from the respective comparable prior year periods primarily due to the development of additional technology and purchases of other assets, particularly with respect to the timing of new buildings and a parking garage that were placed in service in 2018 and 2017, respectively.

Interest Expense

Interest expense for the year ended December 31, 2018 decreased $0.1 million from the prior year primarily due to increased capitalized interest related to the construction of our fourth headquarters building in the first half of 2018. Interest expense for the year ended December 31, 2017 decreased $0.1 million from the comparable prior year period primarily due to an increase in capitalized interest related to the construction of our third and fourth headquarters buildings during 2017.

Other Income, net

For the year ended December 31, 2018, other income, net increased from the prior year by $2.8 million due primarily to the increase in the fair value of our interest rate swap and the loss on early repayment of debt which occurred in 2017. For the year ended December 31, 2017, other income, net decreased $1.4 million compared to the year ended December 31, 2016 primarily due to a $0.9 million loss on early repayment of debt and a $0.6 million unrealized loss recognized on the fair value of an interest rate swap.

Provision for Income Taxes

For the year ended December 31, 2018, income tax expense increased $33.4 million compared to the year ended December 31, 2017. Income tax expense in 2017 was lower due to the enactment of the Tax Cuts and Jobs Act of 2017 (the “Tax Act”) and recognition of excess tax benefits from share-based payment awards due to the vesting of various market-based stock awards during 2017. As a result of the Tax Act, we remeasured certain deferred tax assets and liabilities based on expected future rates. This remeasurement, as adjusted for the adoption of ASU 2014-09, resulted in a $24.9 million benefit to our provision for income taxes for the year ended December 31, 2017.

Liquidity and Capital Resources

Our principal sources of liquidity are cash and cash equivalents, which totaled $45.7 million and $46.1 million as of December 31, 2018 and 2017, respectively. Our cash and cash equivalents are comprised primarily of demand deposit accounts, money market funds and certificates of deposit. We also have the ability to borrow funds pursuant to a senior secured revolving credit facility (the “Facility”) in the aggregate principal amount of $50.0 million, which may be increased up to $100.0 million, subject to obtaining additional lender commitments and certain approvals and satisfying certain other conditions. We believe our existing cash and cash equivalents will be sufficient to meet our working capital and capital expenditure needs over at least the next 12 months.

We have historically financed our operations from cash flows generated from operations, cash from the sale of equity securities and debt financing. Although we have funded most of the costs for ongoing construction projects at our corporate headquarters from available cash, we have incurred indebtedness for a portion of these costs. Further, all purchases under our stock repurchase plans were funded from available cash.

Recent Liquidity Developments

Term Credit Agreement. On December 7, 2017, we entered into a senior secured term credit agreement (“Term Credit Agreement”), pursuant to which JPMorgan Chase Bank, N.A., Bank of America, N.A. and Kirkpatrick Bank have agreed to make certain term loans to us (the “Term Loans”) from time to time during the period beginning December 7, 2017 and ending September 7, 2018 (the “Term Loan Draw Expiration Date”) in an aggregate principal amount of up to $60.0 million. On September 12, 2018, we entered into the First Amendment to the Term Credit Agreement (the

"Amendment") dated effective as of September 7, 2018, which extended the Term Loan Draw Expiration Date to March 7, 2019. As of December 31, 2018, our indebtedness of $34.4 million consisted solely of Term Loans made under the Term Credit Agreement.

There was $24.5 million of borrowing capacity remaining under the Term Credit Agreement as of December 31, 2018. Our obligations under the Term Loans are secured by a mortgage and first priority security interest in our headquarters property. Term Loans made after December 7, 2017 may be used to finance hard and soft costs related to the completion of construction of our fourth headquarters building and any landscaping, groundwork, parking lots and roads reasonably incidental thereto. The Term Loans mature on September 7, 2025 and bear interest, at our option, at either (a) a prime rate plus 1.0% or (b) an adjusted LIBOR rate for the interest period in effect for such Term Loan plus 1.5%. The adjusted LIBOR rate is equal to (i) the LIBOR rate for the applicable interest period multiplied by (ii) the statutory reserve rate (equal to (x) one divided by (y) one minus the aggregate of the maximum reserve percentage (including any marginal, special, emergency or supplemental reserves) established by the Board of Governors of the Federal Reserve System of the United States).

Under the Term Credit Agreement, we are required to comply with certain financial and non-financial covenants, including maintaining a fixed charge coverage ratio of not less than 1.25 to 1.0 and a funded indebtedness to EBITDA ratio of not greater than 2.0 to 1.0. Additionally, the Term Credit Agreement contains customary affirmative and negative covenants, including covenants limiting our ability to, among other things, grant liens, incur debt, effect certain mergers, make investments, dispose of assets, enter into certain transactions, including swap agreements and sale and leaseback transactions, pay dividends or distributions on their capital stock, and enter into transactions with affiliates, in each case subject to customary exceptions for a credit agreement of this size and type. As of December 31, 2018, we were in compliance with all covenants set forth in the Term Credit Agreement.

In connection with entering into the Term Credit Agreement, we also entered into a floating-to-fixed interest rate swap agreement to limit the exposure to interest rate risk related to the Term Loans (the "Interest Rate Swap Agreement"). The Interest Rate Swap Agreement, which has a maturity date of September 7, 2025, provides that we will receive quarterly variable interest payments based on the LIBOR rate and will pay interest at a fixed rate. We have elected not to designate this interest rate swap as a hedge and, as such, changes in the fair value of the derivative instrument are recognized in our consolidated statements of income. For the years ended December 31, 2018 and 2017, we recognized a gain of $0.7 million and a loss of $0.6 million, respectively, for the change in fair value of the interest rate swap, which is included in Other income, net in the consolidated statements of income.

Revolving Credit Agreement. On February 12, 2018, we entered into a senior secured revolving credit agreement (the "Revolving Credit Agreement") with JPMorgan Chase Bank, N.A. and Bank of America, N.A. which provides for the Facility in the aggregate principal amount of $50.0 million, which may be increased to up to $100.0 million, subject to obtaining additional lender commitments and certain approvals and satisfying certain other conditions. The Facility includes a $5.0 million sublimit for swingline loans and a $2.5 million sublimit for letters of credit. The Facility is scheduled to mature on February 12, 2020. Borrowings under the Facility will generally bear interest at a prime rate plus 1.0% or, at our option, an adjusted LIBOR rate for the interest period in effect for such borrowing plus 1.5%, in each case subject to certain conditions set forth in the Revolving Credit Agreement. The Revolving Credit Agreement also contains financial and non-financial covenants that are substantially similar to the covenants in the Term Credit Agreement described above. The proceeds from the loans under the Facility are to be used for working capital and general business purposes. Letters of credit are to be used to support our business operations. As of December 31, 2018, we did not have any borrowings outstanding under the Facility. As of December 31, 2018, we were in compliance with all covenants set forth in the Revolving Credit Agreement.

Stock Repurchase Plan. In May 2016, our Board of Directors authorized a stock repurchase plan allowing for the repurchase of shares of our common stock in open market transactions at prevailing market prices, in privately negotiated transactions or by other means in accordance with federal securities laws, including Rule 10b5-1 programs. Since the initial authorization of the stock repurchase plan, our Board of Directors has amended and extended the stock repurchase plan from time to time. On February 13, 2018, we announced our Board of Directors authorized the repurchase of up to an additional $100.0 million of common stock. Most recently, on November 20, 2018, we announced our Board of Directors authorized the repurchase of up to an additional $150.0 million of our common stock. Our stock repurchase plan may be suspended or discontinued at any time. The actual timing, number and value of shares repurchased depends on a number of factors, including the market price of our common stock, general market and economic conditions, the shares withheld for taxes associated with the vesting of restricted stock and other corporate considerations.

During the year ended December 31, 2018, we repurchased an aggregate of 1,108,885 shares of common stock for an aggregate cost of $125.4 million, including 186,165 shares to satisfy tax withholding obligations for certain employees upon the vesting of restricted stock, as discussed below. As of December 31, 2018, there was $162.0 million available for repurchases. The stock repurchase plan will expire on November 19, 2020.

Withholding Shares to Cover Taxes. During the year ended December 31, 2018, we withheld 186,165 shares to satisfy tax withholding obligations with respect to the delivery of vested shares of restricted stock to certain employees. Our payment of the taxes on behalf of those employees resulted in a cash expenditure of $20.2 million and, as such, we generally subtract the amounts attributable to such withheld shares from the aggregate amount available for future purchases under our stock repurchase plan.

Cash Flow Analysis

Our cash flows from operating activities have historically been significantly impacted by profitability, implementation revenues received but deferred, our investments in sales and marketing initiatives to drive growth, and research and development. Our ability to meet future liquidity needs will be driven by our operating performance and the extent of continued investment in our operations. Failure to generate sufficient revenues and related cash flows could have a material adverse effect on our ability to meet our liquidity needs and achieve our business objectives.

As our business grows, we expect our capital expenditures and our investment activity to continue to increase. Although we completed construction of our fourth headquarters building in the second quarter of 2018, we are now focused on the planning and design of our new Texas operations facility in Grapevine, Texas. Capital expenditures related to the construction of the facility are expected to begin in the first half of 2019. For the year ending December 31, 2019, we expect capital expenditures, as a percentage of total revenues, to be consistent with capital expenditures for the year ended December 31, 2018. Depending on certain growth opportunities, we may choose to accelerate investments in sales and marketing, acquisitions, technology and services. Actual future capital requirements will depend on many factors, including our future revenues, cash from operating activities and the level of expenditures in all areas of our business.

As part of our payroll and payroll tax filing services, we collect funds from our clients for federal, state and local employment taxes, which we remit to the appropriate tax authorities. We invest these funds in money market funds, demand deposit accounts, commercial paper and certificates of deposit from which we earn interest income during the period between their receipt and disbursement.

Our cash flows from investing and financing activities are influenced by the amount of funds held for clients, which can vary significantly from quarter to quarter. The balance of the funds we hold depends on our clients' payroll calendars, and therefore such balance changes from period to period in accordance with the timing of each payroll cycle.

Our cash flows from financing activities are also affected by the extent to which we use available cash to purchase shares of common stock under our stock repurchase plan as well as restricted stock vesting events that result in net share settlements and the Company paying withholding taxes on behalf of certain employees.

The following table summarizes the consolidated statements of cash flows for the years ended December 31, 2018, 2017 and 2016:

	Year Ended December 31,			$ Change 2018 vs 2017	% Change 2018 vs 2017	$ Change 2017 vs 2016	% Change 2017 vs 2016
	2018	2017	2016				
	(dollars in thousands)						
Net cash provided by (used in):							
Operating activities	$184,817	$130,149	$98,818	$54,668	42 %	$31,331	32 %
Investing activities	62,620	(289,895)	(204,916)	352,515	-122 %	(84,979)	41 %
Financing activities	(247,796)	145,665	115,542	(393,461)	-270 %	30,123	26 %
Change in cash and cash equivalents	$(359)	$(14,081)	$9,444	$13,722	-97 %	$(23,525)	-249 %

Operating Activities

Cash provided by operating activities for the year ended December 31, 2018 primarily consisted of payments received from our clients and interest earned on funds held for clients. Cash used in operating activities primarily consisted of personnel-related expenditures to support the growth and infrastructure of our business. These payments included costs of operations, advertising and other sales and marketing efforts, IT infrastructure development, product research and development and security and administrative costs. Compared to the year ended December 31, 2017, our operating cash flows for the year ended December 31, 2018 were positively impacted by the growth of our business.

Investing Activities

Cash flows from investing activities for the year ended December 31, 2018 increased from the prior year period due to the impact of $417.5 million of changes in funds held for clients and a $14.3 million increase in proceeds from maturities of short-term investments from funds held for clients, partially offset by a $78.8 million increase in purchases of short-term investments from funds held for clients and a $0.5 million increase in cash used for purchases of property and equipment primarily related to the development of additional technology and purchases of other assets.

Cash flows from investing activities for the year ended December 31, 2017 decreased from the prior year period due to the impact of $241.7 million of changes in funds held for clients, a $15.6 million increase in purchases of property and equipment and a $0.3 million decrease in proceeds from sale of property and equipment, partially offset by a $125.1 million increase in proceeds from maturities of short-term investments from funds held for clients and a $47.6 million decrease in purchases of short-term investments from funds held for clients.

Financing Activities

Cash flows from financing activities for the year ended December 31, 2018 decreased from the prior year period due to the impact of $352.4 million of changes in client funds obligation, which is due to the timing of receipts from our clients and payments made to our clients' employees and applicable taxing authorities on their behalf. Financing cash flows were also impacted by a $48.3 million increase in open market repurchases of common stock and a $40.9 million decrease in proceeds from the issuance of long-term debt. These cash flows used in financing activities were partially offset by a $34.4 million decrease in principal payments on long-term debt, a $12.6 million decrease in withholding taxes paid related to net share settlements, a $0.8 million decrease in debt extinguishment costs and a $0.3 million decrease in the payment of debt issuance costs.

Cash flows from financing activities for the year ended December 31, 2017 increased from the prior year period due to the impact of $69.4 million of changes in client funds obligation, which is due to the timing of receipts from our clients and payments made to our clients' employees and applicable taxing authorities on their behalf. Financing cash flows were also impacted by the $35.9 million increase in proceeds from the issuance of long-term debt. These cash flows provided by financing activities were partially offset by the $34.4 million increase in principal payments on long-term debt related to our previous loan agreements, a $21.3 million increase in open market repurchases of common stock, an $18.4 million increase in withholding taxes paid related to net share settlements, $0.8 million in debt extinguishment costs and a $0.3 million increase in the payment of debt issuance costs.

Contractual Obligations

Our principal commitments primarily consist of long-term debt and leases for office space. We disclose our long-term debt in Note 5 and our commitments and contingencies in Note 12 in our consolidated financial statements included elsewhere in this Form 10-K.

As of December 31, 2018, the future non-cancelable minimum payments under these commitments were as follows:

		Payments Due by Period			
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Long-term debt obligations:					
Net term notes to bank due September 7, 2025	$34,613	$1,775	$3,550	$3,550	25,738
Interest on net term notes to bank due September 7, 2025	7,613	1,370	2,527	2,227	1,489
Operating lease obligations:					
Facilities space	28,258	8,315	12,124	7,317	502
Total	$70,484	$11,460	$18,201	$13,094	$27,729

We plan to continue to lease additional office space to support our growth. In addition, many of our existing lease agreements provide us with the option to renew. When applicable, our future operating lease obligations include payments due during any renewal period provided for in the lease where the lease imposes a penalty for failure to renew.

The contractual commitment amounts in the table above are associated with agreements that are enforceable and legally binding and that specify all significant terms, including fixed or minimum services to be used, fixed minimum or variable price provisions, and the approximate timing of the transaction. Obligations under contracts that we can cancel without a significant penalty are not included in the table above.

Off-Balance Sheet Arrangements

As of December 31, 2018, we did not have any off-balance sheet arrangements that have or are reasonably likely to have an effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that may be material to investors.

Critical Accounting Policies and Estimates

Our consolidated financial statements and accompanying notes have been prepared in accordance with U.S. GAAP. The preparation of these consolidated financial statements requires us to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses, and related disclosures. On an ongoing basis, we continually evaluate our estimates and assumptions believed to be reasonable under current facts and circumstances. Actual amounts and results may materially differ from these estimates made by management under different assumptions and conditions.

Certain accounting policies that require significant management estimates, and are deemed critical to our results of operations or financial position, are described below. Accordingly, these are the policies we believe are the most critical to aid in fully understanding and evaluating our consolidated financial condition and results of operations.

Revenue Recognition

Revenues are recognized when control of the promised goods or services is transferred to our clients in an amount that reflects the consideration we expect to be entitled to for those goods or services. Substantially all of our revenues are comprised of revenue from contracts with clients. Sales and other applicable taxes are excluded from revenues.

Recurring revenues are derived primarily from our talent acquisition, time and labor management, payroll, talent management and HR management applications as well as fees charged for form filings and delivery of client payroll checks and reports. Talent acquisition includes our applicant tracking, candidate tracker, background check, on-boarding, e-verify and tax credit services applications. Time and labor management includes time and attendance, scheduling/schedule exchange, time-off requests, labor allocation, labor management reports/push reporting and geofencing/geotracking. Payroll includes our payroll and tax management, Paycom Pay, expense management, garnishment management and GL Concierge applications. Talent management includes our employee self-service, compensation budgeting, performance management, executive dashboard and Paycom learning and course content applications. HR management includes our document and task management, government and compliance, benefits administration, COBRA administration, personnel action forms, surveys and enhanced ACA applications.

The performance obligations related to recurring revenues are satisfied during each client's payroll period, with the agreed-upon fee being charged and collected as part of our processing of the client's payroll. Recurring revenues are recognized at the conclusion of processing of each client's payroll period, when each respective payroll client is billed. Collectability is reasonably assured as the fees are collected through an automated clearing house as part of the client's payroll cycle or through direct wire transfer, which minimizes the default risk.

The contract period for substantially all contracts associated with these revenues is one month due to the fact that both we and the client have the unilateral right to terminate a wholly unperformed contract without compensating the other party by providing 30 days' notice of termination. Our payroll application is the foundation of our solution, and all of our clients are required to utilize this application in order to access our other applications. For clients who purchase multiple applications, due to the short-term nature of our contracts, we do not believe it is meaningful to separately assess and identify whether or not each application potentially represents its own, individual, performance obligation as the revenue generated from each application is recognized within the same month as the revenue from the core payroll application. Similarly, we do not believe it is meaningful to individually determine the standalone selling price for each application. We consider the total price charged to a client in a given period to be indicative of the standalone selling price, as the total amount charged is within a reasonable range of prices typically charged for our goods and services for comparable classes of client groups.

Implementation and other revenues consist of nonrefundable upfront conversion fees which are charged to new clients to offset the expense of new client set-up as well as revenues from the sale of time clocks as part of our employee time and attendance services. Although these revenues are related to our recurring revenues, they represent distinct performance obligations.

Implementation activities primarily represent administrative activities that allow us to fulfill future performance obligations for our clients and, for accounting recognition purposes, do not represent services transferred to the client. However, the nonrefundable upfront fee charged to our clients results in an implied performance obligation in the form of a material right to the client related to the client's option to renew at the end of each 30-day contract period. Further, given that all other services within the contract are sold at a total price indicative of the standalone selling price, coupled with the fact that the upfront fees are consistent with upfront fees charged in similar contracts that we have with clients, the standalone selling price of the client's option to renew approximates the dollar amount of the nonrefundable upfront fee. The nonrefundable upfront fee is typically included on the client's first invoice, and is deferred and recognized ratably over the estimated renewal period (i.e. the ten-year estimated client life).

Revenue from the sale of time clocks is recognized when control is transferred to the client upon delivery of the product. We estimate the standalone selling price for the time clocks by maximizing the use of observable inputs such as our specific pricing practices for time clocks.

Goodwill and Other Intangible Assets

Goodwill is not amortized, but we are required to test the carrying value of goodwill for impairment at least annually, or earlier if, at the reporting unit level, an indicator of impairment arises. The estimates and assumptions about future results of operations and cash flows made in connection with the impairment testing could differ from future actual results of operations and cash flows. If impairment exists, a write-down to fair value is recorded. Our business is largely homogeneous and, as a result, goodwill is associated with one reporting unit. We have selected June 30 as our annual goodwill impairment testing date and determined there was no impairment as of June 30, 2018. For the years ended December 31, 2018, 2017 and 2016, there were no indicators of impairment. Intangible assets with definite lives are amortized on a straight-line basis over their estimated useful lives.

Impairment of Long-Lived Assets

Long-lived assets, including intangible assets with finite lives, are reviewed for impairment when events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the estimated fair value of the asset. We have determined that there is no impairment of long-lived assets for the years ended December 31, 2018, 2017 and 2016.

Restricted Stock

We measure non-cash stock-based compensation expense based on the fair value of the award on the date of grant. We determine the fair value of stock awards issued by using a Monte Carlo simulation model. This model considers various subjective assumptions as inputs, and represent our best estimates, which involve inherent uncertainties and the application of our judgment as it relates to market volatilities, the historical volatility of our stock price, risk-free rates and expected life. The valuation model also incorporates exercise and forfeiture assumptions based on an analysis of historical data. Determining these assumptions is subjective and complex, and therefore, a change in the assumptions utilized could impact the calculation of the fair value of our stock awards and the associated compensation expense. Refer to Note 10 in the notes to our consolidated financial statements for further information regarding our stock-based compensation awards.

Recent Accounting Pronouncements

Refer to Note 2 in the notes to the consolidated financial statements for a full description of recent accounting pronouncements.

Non-GAAP Financial Measures

Management uses adjusted EBITDA and non-GAAP net income as supplemental measures to review and assess the performance of our core business operations and for planning purposes. We define (i) adjusted EBITDA as net income plus interest expense, taxes, depreciation and amortization, non-cash stock-based compensation expense, loss on early repayment of debt, certain transaction expenses that are not core to our operations and the change in fair value of our interest rate swap and (ii) non-GAAP net income as net income plus non-cash stock-based compensation expense, certain transaction expenses that are not core to our operations, loss on early repayment of debt and the change in fair value of our interest rate swap, all of which are adjusted for the effect of income taxes. Adjusted EBITDA and non-GAAP net income are metrics that provide investors with greater transparency to the information used by management in its financial and operational decision-making. We believe these metrics are useful to investors because they facilitate comparisons of our core business operations across periods on a consistent basis, as well as comparisons with the results of peer companies, many of which use similar non-GAAP financial measures to supplement results under U.S. GAAP. In addition, adjusted EBITDA is a measure that provides useful information to management about the amount of cash available for reinvestment in our business, repurchasing common stock and other purposes. Management believes that the non-GAAP measures presented in this Form 10-K, when viewed in combination with our results prepared in accordance with U.S. GAAP, provide a more complete understanding of the factors and trends affecting our business and performance.

Adjusted EBITDA and non-GAAP net income are not measures of financial performance under U.S. GAAP, and should not be considered a substitute for net income, which we consider to be the most directly comparable U.S. GAAP measure. Adjusted EBITDA and non-GAAP net income have limitations as analytical tools, and when assessing our operating performance, you should not consider adjusted EBITDA or non-GAAP net income in isolation, or as a substitute for net income or other consolidated statements of income data prepared in accordance with U.S. GAAP. Adjusted EBITDA and non-GAAP net income may not be comparable to similar titled measures of other companies and other companies may not calculate such measures in the same manner as we do.

The following tables reconcile net income to adjusted EBITDA, net income to non-GAAP net income and earnings per share to non-GAAP net income per share on a basic and diluted basis:

	Year Ended December 31,		
	2018	2017 *As Adjusted	2016 *As Adjusted
	(in thousands)		
Net income to adjusted EBITDA:			
Net income	$137,065	$123,486	$70,421
Interest expense	766	911	1,036
Provision for income taxes	37,646	4,246	30,591
Depreciation and amortization	29,657	19,395	13,632
EBITDA	205,134	148,038	115,680
Non-cash stock-based compensation expense	36,411	36,047	20,796
Loss on early repayment of debt	—	923	—
Change in fair value of interest rate swap	(667)	649	—
Adjusted EBITDA	$240,878	$185,657	$136,476

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 in the notes to our consolidated financial statements for a description of adjustments.

	Year Ended December 31,		
	2018	2017 *As Adjusted	2016 *As Adjusted
	(in thousands, except share and per share amounts)		
Net income to non-GAAP net income:			
Net income	$137,065	$123,486	$70,421
Non-cash stock-based compensation expense	36,411	36,047	20,796
Loss on early repayment of debt	—	923	—
Change in fair value of interest rate swap	(667)	649	—
Income tax effect on non-GAAP adjustments	(16,197)	(28,795)	(14,125)
Non-GAAP net income	$156,612	$132,310	$77,092
Earnings per share, basic	$2.37	$2.13	$1.21
Earnings per share, diluted	$2.34	$2.10	$1.19
Non-GAAP net income per share, basic	$2.71	$2.29	$1.34
Non-GAAP net income per share, diluted	$2.67	$2.25	$1.31
Weighted average shares outstanding:			
Basic	57,711,315	57,839,155	57,550,204
Diluted	58,582,486	58,790,019	58,968,099

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 in the notes to our consolidated financial statements for a description of adjustments.

	Year Ended December 31,		
	2018	2017 *As Adjusted	2016 *As Adjusted
Earnings per share to non-GAAP net income per share, basic:			
Earnings per share, basic	$2.37	$ 2.13	$ 1.21
Non-cash stock-based compensation expense	0.63	0.62	0.36
Loss on early repayment of debt	—	0.02	—
Change in fair value of interest rate swap	(0.01)	0.01	—
Income tax effect on non-GAAP adjustments	(0.28)	(0.49)	(0.23)
Non-GAAP net income per share, basic	$2.71	$ 2.29	$ 1.34

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 in the notes to our consolidated financial statements for a description of adjustments.

	Year Ended December 31,		
	2018	2017 *As Adjusted	2016 *As Adjusted
Earnings per share to non-GAAP net income per share, diluted:			
Earnings per share, diluted	$2.34	$ 2.10	$ 1.19
Non-cash stock-based compensation expense	0.62	0.61	0.35
Loss on early repayment of debt	—	0.02	—
Change in fair value of interest rate swap	(0.01)	0.01	—
Income tax effect on non-GAAP adjustments	(0.28)	(0.49)	(0.23)
Non-GAAP net income per share, diluted	$2.67	$ 2.25	$ 1.31

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 in the notes to our consolidated financial statements for a description of adjustments.

Item 7A.Quantitative and Qualitative Disclosures about Market Risk

Interest rate sensitivity

Cash and cash equivalents totaled $45.7 million as of December 31, 2018. These amounts are invested primarily in demand deposit accounts, money market funds and certificates of deposit. We consider all highly liquid debt instruments purchased with a maturity of three months or less and SEC-registered money market mutual funds to be cash equivalents. The primary objectives of our investing activities are capital preservation, meeting our liquidity needs and, with respect to investing client funds, generating interest income while maintaining the safety of principal. We do not enter into investments for trading or speculative purposes.

Our cash equivalents are subject to market risk due to changes in interest rates. The market value of fixed rate securities may be adversely affected due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations due to changes in interest rates, or we may suffer losses in principal if we are forced to sell securities that decline in market value due to changes in interest rates.

As of December 31, 2018, an increase or decrease in interest rates of 100-basis points would not have had a material effect on our operating results or financial condition.

In December 2017, we entered into the Term Credit Agreement, pursuant to which the lenders parties thereto have agreed to make Term Loans to us in an aggregate principal amount of up to $60.0 million, which will mature on September 7, 2025. As described elsewhere in this Form 10-K, the Term Loans bear interest, at our option, at either (a) a prime rate plus 1.0% or (b) an adjusted LIBOR rate for the interest period in effect for such Term Loan plus 1.5%. As a result, we are exposed to increased interest rate risk. To mitigate the increased interest rate risk, we entered into the Interest Rate Swap Agreement. The Interest Rate Swap Agreement has effectively fixed our rate at 4.0%, eliminating a portion of the variable rate and coinciding interest rate risk associated with the Term Loans.

In February 2018, we entered into the Revolving Credit Agreement, which provides for a credit facility in the aggregate amount of $50.0 million, which may be increased to up to $100.0 million, subject to obtaining additional lender commitments and certain approvals and satisfying certain other conditions. As described elsewhere in this Form 10-K, borrowings under the Facility will generally bear interest at a prime rate plus 1.0% or, at our option, an adjusted LIBOR rate for the interest period in effect for such borrowing plus 1.5%. As of December 31, 2018, we did not have any borrowings outstanding under the Facility. To the extent we make draws under the Facility in the future, we may be exposed to increased interest rate risk.

Item 8. Financial Statements and Supplementary Data

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders

Paycom Software, Inc.

Opinion on the financial statements

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

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in the 2013 Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"), and our report dated February 14, 2019 expressed an unqualified opinion.

Change in Accounting Principle

As discussed in Note 2 of the consolidated financial statements, the Company has changed its method of accounting for certain costs to obtain new contracts and costs to fulfill contracts in 2018 due to the adoption of the new revenue recognition standard and the codification of guidance on other assets and deferred costs related to contracts with customers.

Basis for opinion

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

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

/s/ GRANT THORNTON LLP

We have served as the Company's auditor since 2009.

Oklahoma City, Oklahoma

February 14, 2019

Paycom Software, Inc.

Consolidated Balance Sheets

(in thousands, except share amounts)

	December 31,	
	2018	2017 *As Adjusted
Assets		
Current assets:		
Cash and cash equivalents	$45,718	$46,077
Accounts receivable	3,414	1,576
Prepaid expenses	7,658	4,982
Inventory	797	979
Income tax receivable	3,962	7,047
Deferred contract costs	35,286	26,403
Current assets before funds held for clients	96,835	87,064
Funds held for clients	967,787	1,089,201
Total current assets	1,064,622	1,176,265
Property and equipment, net	176,962	147,705
Deposits and other assets	2,249	1,456
Goodwill	51,889	51,889
Intangible assets, net	745	958
Long-term deferred contract costs	225,459	171,865
Total assets	$1,521,926	$1,550,138
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$6,288	$6,490
Accrued commissions and bonuses	10,671	9,585
Accrued payroll and vacation	10,741	7,015
Deferred revenue	8,980	6,982
Current portion of long-term debt	1,775	888
Accrued expenses and other current liabilities	22,440	19,991
Current liabilities before client funds obligation	60,895	50,951
Client funds obligation	967,787	1,089,201
Total current liabilities	1,028,682	1,140,152
Deferred income tax liabilities, net	70,206	49,129
Long-term derivative liability	—	554
Long-term deferred revenue	55,671	44,642
Net long-term debt, less current portion	32,614	34,414
Total long-term liabilities	158,491	128,739
Total liabilities	1,187,173	1,268,891
Commitments and contingencies (Note 12)		
Stockholders' equity:		
Common stock, $0.01 par value (100,000,000 shares authorized, 60,746,715 and 60,149,411 shares issued at December 31, 2018 and 2017, respectively; 57,276,992 and	607	601

57,788,573 shares outstanding at December 31, 2018 and 2017, respectively)		
Additional paid in capital	203,680	161,809
Retained earnings	395,590	258,525
Treasury stock, at cost (3,469,723 and 2,360,838 shares at December 31, 2018 and 2017, respectively)	(265,124)	(139,688)
Total stockholders' equity	334,753	281,247
Total liabilities and stockholders' equity	$1,521,926	$1,550,138

*Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

See accompanying notes to the consolidated financial statements.

Paycom Software, Inc.

Consolidated Statements of Income

(in thousands, except share and per share amounts)

	Year Ended December 31,		
	2018	2017 *As Adjusted	2016 *As Adjusted
Revenues			
Recurring	$557,255	$425,424	$323,548
Implementation and other	9,081	7,623	5,593
Total revenues	566,336	433,047	329,141
Cost of revenues			
Operating expenses	76,231	62,438	48,268
Depreciation and amortization	14,532	9,590	5,798
Total cost of revenues	90,763	72,028	54,066
Administrative expenses			
Sales and marketing	143,881	110,846	85,361
Research and development	46,247	30,430	20,966
General and administrative	96,605	80,228	59,174
Depreciation and amortization	15,125	9,805	7,834
Total administrative expenses	301,858	231,309	173,335
Total operating expenses	392,621	303,337	227,401
Operating income	173,715	129,710	101,740
Interest expense	(766)	(911)	(1,036)
Other income, net	1,762	(1,067)	308
Income before income taxes	174,711	127,732	101,012
Provision for income taxes	37,646	4,246	30,591
Net income	$137,065	$123,486	$70,421
Earnings per share, basic	$2.37	$2.13	$1.21
Earnings per share, diluted	$2.34	$2.10	$1.19
Weighted average shares outstanding:			
Basic	57,711,315	57,839,155	57,550,204
Diluted	58,582,486	58,790,019	58,968,099

*Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

See accompanying notes to the consolidated financial statements.

Paycom Software, Inc.

Consolidated Statements of Stockholders' Equity

(in thousands, except share amounts)

	Common Stock		Additional Paid in Capital *As Adjusted	Retained Earnings *As Adjusted	Treasury Stock		Total Stockholders' Equity *As Adjusted
	Shares	Amount			Shares	Amount	
Balances at December 31, 2015	57,119,873	$ 571	$ 71,135	$ 26,608	—	$—	$ 98,314
Cumulative-effect adjustment to Additional paid in capital and Retained earnings related to the adoption of ASU No. 2016-09 (see Note 2)	—	—	$ 24,575	$ 38,010	—	$—	$ 62,585
Vesting of restricted stock	1,333,410	14	(14)	—	—	—	—
Stock-based compensation	—	—	24,331		—	—	24,331
Repurchases of common stock	—	—	—	—	1,122,261	(49,958)	(49,958)
Net income	—	—	—	70,421	—	—	70,421
Balances at December 31, 2016	58,453,283	$ 585	$ 120,027	$ 135,039	1,122,261	$ (49,958)	$ 205,693
Vesting of restricted stock	1,696,128	16	(16)	—	—	—	—
Stock-based compensation	—	—	41,798	—	—	—	41,798
Repurchases of common stock	—	—	—	—	1,238,577	(89,730)	(89,730)
Net income	—	—	—	123,486	—	—	123,486
Balances at December 31, 2017	60,149,411	$ 601	$ 161,809	$ 258,525	2,360,838	$ (139,688)	$ 281,247
Vesting of restricted stock	597,304	6	(6)	—	—	—	—
Stock-based compensation	—	—	41,877	—	—	—	41,877
Repurchases of common stock	—	—	—	—	1,108,885	(125,436)	(125,436)
Net income	—	—	—	137,065	—	—	137,065
Balances at December 31, 2018	60,746,715	$ 607	$ 203,680	$ 395,590	3,469,723	$ (265,124)	$ 334,753

*Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

See accompanying notes to the consolidated financial statements.

Paycom Software, Inc.

Consolidated Statements of Cash Flows

(in thousands)

	Year Ended December 31,		
		2017	2016
	2018	*As Adjusted	*As Adjusted
Cash flows from operating activities:			
Net income	$137,065	$123,486	$70,421
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	29,657	19,395	13,632
Accretion of discount on available-for-sale securities	(1,112)	(451)	(135)
(Gain)/loss on disposition of property and equipment	—	21	(64)
Amortization of debt discount and debt issuance costs	32	117	124
Stock-based compensation expense	36,576	36,076	20,721
Loss on early repayment of debt	—	923	—
Cash paid for derivative settlement	(188)	(24)	—
(Gain)/loss on derivative	(479)	673	—
Deferred income taxes, net	21,077	(7,681)	15,340
Changes in operating assets and liabilities:			
Accounts receivable	(1,838)	(237)	1,015
Prepaid expenses	(2,676)	(507)	(944)
Inventory	(306)	462	418
Deposits and other assets	(762)	(241)	71
Deferred contract costs	(60,730)	(48,619)	(42,019)
Accounts payable	1,079	79	(1,571)
Income taxes, net	3,085	(6,355)	6,051
Accrued commissions and bonuses	1,086	1,582	(684)
Accrued payroll and vacation	3,726	2,246	1,871
Deferred revenue	13,027	11,913	10,675
Accrued expenses and other current liabilities	6,498	(2,709)	3,896
Net cash provided by operating activities	184,817	130,149	98,818
Cash flows from investing activities:			
Purchase of short-term investments from funds held for clients	(145,011)	(66,235)	(113,792)
Proceeds from maturities of short-term investments from funds held for clients	155,500	141,205	16,135
Net change in funds held for clients	112,037	(305,476)	(63,749)
Purchases of property and equipment	(59,906)	(59,389)	(43,805)
Proceeds from sale of property and equipment	—	—	295
Net cash provided by (used in) investing activities	62,620	(289,895)	(204,916)
Cash flows from financing activities:			
Proceeds from issuance of long-term debt	—	40,940	5,000
Repurchases of common stock	(105,188)	(56,880)	(35,561)
Withholding taxes paid related to net share settlements	(20,248)	(32,850)	(14,396)

Principal payments on long-term debt	(888)	(35,335)	(964)
Net change in client funds obligation	(121,414)	230,957	161,541
Debt extinguishment costs	—	(823)	—
Payment of debt issuance costs	(58)	(344)	(78)
Net cash provided by (used in) financing activities	(247,796)	145,665	115,542
Net change in cash and cash equivalents	(359)	(14,081)	9,444
Cash and cash equivalents			
Beginning of year	46,077	60,158	50,714
End of year	$45,718	$46,077	$60,158

*Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

See accompanying notes to the consolidated financial statements.

Paycom Software, Inc.

Consolidated Statements of Cash Flows, continued

(in thousands)

	Year Ended December 31,		
	2018	2017 *As Adjusted	2016 *As Adjusted
Supplemental disclosures of cash flow information:			
Cash paid for interest, net of amounts capitalized	$708	$ 791	$ 938
Cash paid for income taxes	$13,511	$ 18,332	$ 9,323
Noncash investing and financing activities:			
Purchases of property and equipment, accrued but not paid	$1,759	$ 6,686	$ 4,651
Stock-based compensation for capitalized software	$3,722	$ 3,285	$ 1,784

*Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

See accompanying notes to the consolidated financial statements.

Paycom Software, Inc.

Notes to the Consolidated Financial Statements

1. ORGANIZATION AND DESCRIPTION OF BUSINESS

Description of Business

Paycom Software, Inc. (“Software”) and its wholly owned subsidiaries (collectively, the “Company”) is a leading provider of comprehensive, cloud-based human capital management (“HCM”) software delivered as Software-as-a-Service. Unless we state otherwise or the context otherwise requires, the terms “we”, “our”, “us” and the “Company” refer to Software and its consolidated subsidiaries.

We provide functionality and data analytics that businesses need to manage the complete employment lifecycle from recruitment to retirement. Our solution requires virtually no customization and is based on a core system of record maintained in a single database for all HCM functions, including talent acquisition, time and labor management, payroll, talent management and human resources (“HR”) management applications.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Our consolidated financial statements include the financial results of Software and its wholly owned subsidiaries and have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) and applicable rules and regulations of the Securities and Exchange Commission (“SEC”). Intercompany balances and transactions have been eliminated in consolidation. In the opinion of management, the accompanying consolidated financial statements include all adjustments necessary for the fair presentation for the periods presented. Such adjustments are of a normal recurring nature.

Effective January 1, 2018, we adopted the requirements of Accounting Standards Update (“ASU”) No. 2014-09, “Revenue from Contracts with Customers (Topic 606),” as discussed in Note 2. All amounts and disclosures set forth in this Form 10-K have been updated to comply with this new standard, as indicated by the “as adjusted” footnote in applicable tables within the notes to the consolidated financial statements.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current period presentation. These reclassifications had no impact on reported net income and did not result in any material change to operating cash flows.

Adoption of New Pronouncements

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued ASU No. 2014-09, “Revenue from Contracts with Customers (Topic 606)” (“ASU 2014-09”). This authoritative guidance includes a comprehensive new revenue recognition model that requires revenue to be recognized in a manner to depict the transfer of goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services. ASU 2014-09 also includes Accounting Standards Codification (“ASC”) 340-40, “Other Assets and Deferred Costs – Contracts with Customers” (“ASC 340-40”), which codifies the guidance on other assets and deferred costs relating to contracts with customers. ASC 340-40 specifies the accounting for costs an entity incurs to obtain and fulfill a contract to provide goods and services to customers. We adopted ASU 2014-09 on January 1, 2018, utilizing the full retrospective method of transition, which required us to recast each prior period presented and included a cumulative pre-tax adjustment of $103.4 million as of January 1, 2016. We have also updated our control framework for new internal controls and made changes to existing controls related to the new standard, including certain reconciliation controls, management review controls and contract review controls.

Impact on Previously Reported Results

The provisions of ASU 2014-09 do not materially impact the timing or amount of revenue we recognize. The primary impact of adopting the new standard is the manner in which we account for certain costs to obtain new contracts (i.e., selling and commission costs) and costs to fulfill contracts (i.e., costs related to upfront implementation activities performed), which we had previously expensed as incurred. We also determined that the nonrefundable upfront fee charged to our clients, coupled with the option to renew, represents an implied performance obligation in the form of a material right. However, as these fees are deferred and recognized ratably over the ten-year estimated client life, consistent with our prior accounting policy, there is no change in revenue recognition.

Paycom Software, Inc.

Notes to the Consolidated Financial Statements

The following table presents a recast of selected consolidated statement of income line items after giving effect to the adoption of ASU 2014-09:

	Year Ended December 31, 2017			Year Ended December 31, 2016		
	As previously reported	Adjustments	As Adjusted	As previously reported	Adjustments	As Adjusted
	(in thousands, except per share amounts)					
Administrative expenses						
Sales and marketing	$150,512	$ (39,666)	$110,846	$119,258	$ (33,897)	$85,361
General and administrative	$91,647	$ (11,419)	$80,228	$69,046	$ (9,872)	$59,174
Operating income	$78,625	$ 51,085	$129,710	$57,971	$ 43,769	$101,740
Provision for income taxes	$9,840	$ (5,594)	$4,246	$13,403	$ 17,188	$30,591
Net income	$66,807	$ 56,679	$123,486	$43,840	$ 26,581	$70,421
Earnings per share, basic	$1.15	$ 0.98	$2.13	$0.76	$ 0.45	$1.21
Earnings per share, diluted	$1.13	$ 0.97	$2.10	$0.74	$ 0.45	$1.19

The following table presents a recast of selected consolidated balance sheet line items after giving effect to the adoption of ASU 2014-09:

	December 31, 2017		
	As previously reported	Adjustments	As Adjusted
	(in thousands)		
Assets			
Deferred contract costs	$—	$ 26,403	$26,403
Deferred income tax assets, net	$3,294	$ (3,294)	$—
Long-term deferred contract costs	$—	$ 171,865	$171,865
Liabilities and Stockholders' Equity			
Deferred income tax liabilities, net	$—	$ 49,129	$49,129
Additional paid in capital	$137,234	$ 24,575	$161,809
Retained earnings	$137,255	$ 121,270	$258,525
Total stockholders' equity	$135,402	$ 145,845	$281,247

The following table presents a recast of selected consolidated statement of cash flows line items after giving effect to the adoption of ASU 2014-09:

	Year Ended December 31, 2017			Year Ended December 31, 2016		
	As previously reported	Adjustments	As Adjusted	As previously reported	Adjustments	As Adjusted
	(in thousands)					

Cash flows from operating activities						
Net income	$66,807	$ 56,679	$123,486	$43,840	$ 26,581	$70,421
Stock-based compensation expense	38,542	(2,466)	36,076	22,471	(1,750)	20,721
Deferred income taxes, net	(2,087)	(5,594)	(7,681)	(1,848)	17,188	15,340
Deferred contract costs	—	(48,619)	(48,619)	—	(42,019)	(42,019)
Net cash provided by operating activities	$130,149	$ —	$130,149	$98,818	$ —	$98,818

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant estimates include income taxes, loss contingencies, the useful life of property and equipment and intangible assets, the life of our client relationships, the fair value of our stock-based awards and the fair value of our financial instruments, intangible assets and goodwill. These estimates are based on historical experience, where applicable, and other assumptions that management believes are reasonable under the circumstances. Actual results could materially differ from these estimates.

Paycom Software, Inc.

Notes to the Consolidated Financial Statements

Segment Information

We operate in a single operating segment and a single reporting segment. Operating segments are defined as components of an enterprise about which separate financial information is evaluated regularly by the chief operating decision maker, who is also the chief executive officer in deciding how to allocate resources and assessing performance. Our chief executive officer allocates resources and assesses performance based upon financial information at the consolidated level. As we operate in one operating segment, all required financial segment information is presented in the consolidated financial statements.

Cash Equivalents

We consider all highly liquid instruments purchased with a maturity of three months or less and money market funds to be cash equivalents. We maintain cash and cash equivalents in demand deposit accounts, money market funds, and certificates of deposit, which may not be federally insured. The fair value of our cash and cash equivalents approximates carrying value. We have not experienced any losses in such accounts and do not believe there is exposure to any significant credit risk on such accounts.

Accounts Receivable

We generally collect revenues from our clients through an automatic deduction from the clients' bank accounts at the time payroll processing occurs. Accounts receivable on our consolidated balance sheets consists primarily of revenue fees related to the last business day of the year, which are collected on the following business day. As accounts receivable are collected via automatic deduction on the following business day, the Company has not recognized an allowance for doubtful accounts.

Inventory

Our inventory consists of two types of time clocks, and related clock attachments, sold to clients as part of our time and attendance services. Inventory is stated at the lower of cost or market with cost determined using the first-in first-out (FIFO) cost method.

Time clocks are purchased as finished goods from a third party and as such we do not have any inventory classified as raw materials or work in process inventory. Rental clocks are issued to clients under month-to-month operating leases and are classified as property and equipment. The Company's inventory obsolescence reserve was $0 as of December 31, 2018, 2017 and 2016, respectively.

Property and Equipment

Property and equipment is stated at cost, net of accumulated depreciation and amortization. Depreciation is computed using the straight line method over the estimated useful lives of the assets as follows:

Furniture, fixtures and equipment	5 years
Computer equipment	3 years

Software and capitalized software	3 years
Buildings	30 years
Leasehold improvements	3 - 5 years
Rental clocks	5 years
Vehicles	3 years

Our leasehold improvements are amortized over the shorter of their estimated useful lives or the related lease terms. Costs incurred during construction of long-lived assets are recorded as construction in progress and are not depreciated until the asset is placed in service.

We capitalize interest costs incurred related to construction in progress. For the years ended December 31, 2018, 2017 and 2016, we incurred interest costs of $1.6 million, $1.7 million and $1.3 million, respectively. For the years ended December 31, 2018, 2017 and 2016, interest costs of $0.8 million, $0.8 million and $0.4 million, respectively, were capitalized.

Internal Use Software

Capitalized costs include external direct costs of materials and services associated with developing or obtaining internal use computer software and certain payroll and payroll-related costs for employees who are directly associated with internal use computer software projects. The amount of payroll costs that are capitalized with respect to these employees is limited to the time directly spent on such projects. Expenditures for software purchases and software developed or obtained for internal use are capitalized and amortized over a three-year period on a straight-line basis. Costs associated with preliminary project stage activities, training, maintenance and all other post-implementation stage activities are expensed as incurred. We also expense internal costs related to minor upgrades and enhancements, as it is impractical to separate these costs from normal maintenance activities.

Paycom Software, Inc.

Notes to the Consolidated Financial Statements

The total capitalized payroll costs related to internal use computer software projects was $22.0 million and $15.8 million during the years ended December 31, 2018 and 2017, respectively, are included in property and equipment. Amortization expense of capitalized software costs were $12.5 million, $7.0 million and $3.6 million for the years ended December 31, 2018, 2017 and 2016, respectively.

Derivatives

In December 2017, we entered into a floating-to-fixed rate swap agreement to limit the exposure to interest rate risk related to our debt. Our interest rate swap effectively converts a portion of the variable interest rate payments to fixed interest rate payments. We do not hold derivative instruments for trading or speculative purposes. The Company has not elected to designate the interest rate swap as a hedge. Changes in the fair value of the derivative are recognized in our consolidated statements of income.

Goodwill and Other Intangible Assets

Goodwill is not amortized, but is instead tested for impairment annually, or earlier if, at the reporting unit level, an indicator of impairment arises. The estimates and assumptions about future results of operations and cash flows made in connection with the impairment testing could differ from future actual results of operations and cash flows. If impairment exists, a write-down to fair value is recognized. Our business is largely homogeneous and, as a result, goodwill is associated with one reporting unit. We have selected June 30 as our annual goodwill impairment testing date and determined there was no impairment as of June 30, 2018. For the years ended December 31, 2018, 2017 and 2016, there were no indicators of impairment. Intangible assets with definite lives are amortized on a straight-line basis over their estimated useful lives.

Impairment of Long-Lived Assets

Long-lived assets, including intangible assets with definite lives, are reviewed for impairment when events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the estimated fair value of the asset. We have determined that there was no impairment of long-lived assets including intangible assets with definite lives, for the years ended December 31, 2018, 2017 and 2016.

Funds Held for Clients and Client Funds Obligation

As part of our payroll and tax filing application, we (i) collect client funds to satisfy their respective federal, state and local employment tax obligations, (ii) remit such funds to the appropriate taxing authorities and accounts designated by our clients, and (iii) manage client tax filings and any related correspondence with taxing authorities. Amounts collected by us from clients for their federal, state and local employment taxes are invested by us, and we earn interest on these funds during the interval between receipt and disbursement.

These investments are shown in our consolidated balance sheets as funds held for clients, and the offsetting liability for the tax filings is shown as client funds obligation. The liability is recorded in the accompanying balance sheets at the time we obtain the funds from clients. The client funds obligation represents liabilities that will be repaid within one year of the balance sheet date. As of December 31, 2018 and 2017, the funds held for clients were invested in money market funds, demand deposit accounts, commercial paper and certificates of deposit. Short-term investments in commercial paper and certificates of deposit with an original maturity duration greater than three months are classified as available-for-sale securities, and are also included within the funds held for clients line item on the balance sheet. These available-for-sale securities are recorded on the balance sheet at fair value, which approximates the amortized cost of the securities. Funds held for clients are classified as a current asset in the consolidated balance sheets because the funds are held solely to satisfy the client funds obligation.

Stock Repurchase Plan

In May 2016, our Board of Directors authorized a stock repurchase plan allowing for the repurchase of shares of our common stock in open market transactions at prevailing market prices, in privately negotiated transactions or by other means in accordance with federal securities laws, including Rule 10b5-1 programs. Since the initial authorization of the stock repurchase plan, our Board of Directors has amended and extended and authorized new stock repurchase plans from time to time. On February 13, 2018, we announced that our Board of Directors authorized the repurchase of up to an additional $100.0 million of common stock. Most recently, on November 20, 2018, we announced that our Board of Directors authorized the repurchase of up to an additional $150.0 million of our common stock. As of December 31, 2018, there was $162.0 million available for repurchases. Our stock repurchase plan may be suspended or discontinued at any time. The actual timing, number and value of shares repurchased depends on a number of factors, including the market price of our common stock, general market and economic conditions, shares withheld for taxes associated with the vesting of restricted stock and other corporate considerations.

Paycom Software, Inc.

Notes to the Consolidated Financial Statements

During the year ended December 31, 2018, we repurchased an aggregate of 1,108,885 shares of our common stock at an average cost of $113.12 per share, including 186,165 shares withheld to satisfy tax withholding obligations for certain employees upon the vesting of restricted common stock. During the year ended December 31, 2017, we repurchased an aggregate of 1,238,577 shares of our common stock at an average cost of $72.45 per share, including 464,302 shares withheld to satisfy tax withholding obligations for certain employees upon the vesting of restricted common stock.

Revenue Recognition

Revenues are recognized when control of the promised goods or services is transferred to our clients in an amount that reflects the consideration we expect to be entitled to for those goods or services. Substantially all of our revenues are comprised of revenue from contracts with clients. Sales tax and other applicable taxes are excluded from revenues. The following table disaggregates revenue by recurring and implementation and other revenues, which represent the major categories of revenues:

	Year Ended December 31,		
	2018	2017	2016
	(in thousands)		
Revenues			
Recurring	$557,255	$425,424	$323,548
Implementation and other	9,081	7,623	5,593
Total revenues	$566,336	$433,047	$329,141

Recurring Revenues

Recurring revenues are derived primarily from our talent acquisition, time and labor management, payroll, talent management and HR management applications as well as fees charged for form filings and delivery of client payroll checks and reports. Talent acquisition includes our applicant tracking, candidate tracker, background check, on-boarding, e-verify and tax credit services applications. Time and labor management includes time and attendance, scheduling/schedule exchange, time-off requests, labor allocation, labor management reports/push reporting and geofencing/geotracking. Payroll includes our payroll and tax management, Paycom Pay, expense management, garnishment management and GL Concierge applications. Talent management includes our employee self-service, compensation budgeting, performance management, executive dashboard and Paycom learning and course content applications. HR management includes our document and task management, government and compliance, benefits administration, COBRA administration, personnel action forms, surveys and enhanced Affordable Care Act applications.

The performance obligations related to recurring revenues are satisfied during each client’s payroll period, with the agreed-upon fee being charged and collected as part of our processing of the client’s payroll. Recurring revenues are recognized at the conclusion of processing of each client’s payroll period, when each respective payroll client is billed. Collectability is reasonably assured as the fees are collected through an automated clearing house as part of the client’s payroll cycle or through direct wire transfer, which minimizes the default risk.

The contract period for substantially all contracts associated with these revenues is one month due to the fact that both we and the client have the unilateral right to terminate a wholly unperformed contract without compensating the other party by providing 30 days' notice of termination. Our payroll application is the foundation of our solution, and all of our clients are required to utilize this application in order to access our other applications. For clients who purchase multiple applications, due to the short-term nature of our contracts, we do not believe it is meaningful to separately assess and identify whether or not each application potentially represents its own, individual, performance obligation as the revenue generated from each application is recognized within the same month as the revenue from the core payroll application. Similarly, we do not believe it is meaningful to individually determine the standalone selling price for each application. We consider the total price charged to a client in a given period to be indicative of the standalone selling price, as the total amount charged is within a reasonable range of prices typically charged for our goods and services for comparable classes of client groups.

Implementation and Other Revenues

Implementation and other revenues consist of nonrefundable upfront conversion fees which are charged to new clients to offset the expense of new client set-up as well as revenues from the sale of time clocks as part of our employee time and attendance services. Although these revenues are related to our recurring revenues, they represent distinct performance obligations.

Implementation activities primarily represent administrative activities that allow us to fulfill future performance obligations for our clients and do not represent services transferred to the client. However, the nonrefundable upfront fee charged to our clients results in an implied performance obligation in the form of a material right to the client related to the client's option to renew at the

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end of each 30-day contract period. Further, given that all other services within the contract are sold at a total price indicative of the standalone selling price, coupled with the fact that the upfront fees are consistent with upfront fees charged in similar contracts that we have with clients, the standalone selling price of the client's option to renew the contract approximates the dollar amount of the nonrefundable upfront fee. The nonrefundable upfront fee is typically included on the client's first invoice, and is deferred and recognized ratably over the estimated renewal period (i.e. the ten-year estimated client life).

Revenues from the sale of time clocks are recognized when control is transferred to the client upon delivery of the product. We estimate the standalone selling price for the time clocks by maximizing the use of observable inputs such as our specific pricing practices for time clocks.

Contract Balances

The timing of revenue recognition for recurring services is consistent with the invoicing of clients as they both occur during the respective client payroll period for which the services are provided. Therefore, we do not recognize a contract asset or liability resulting from the timing of revenue recognition and invoicing. We have elected to apply the practical expedient not to disclose the value of unsatisfied performance obligations for contracts that are less than one year in length. For these contracts, we determined that the core, non-material right, performance obligations are generally satisfied in full by the end of each reporting period as most of our contracts with clients start at the beginning of a calendar month. However, this expedient cannot be applied to initial 30-day contracts with a client that also contain an implied performance obligation in the form of a material right as the material right performance obligation is being recognized over the expected client life which exceeds one year. For the material right performance obligation, as discussed above, we defer the amounts allocated and recognize them ratably over the estimated client life of ten years. Finally, we have also elected to apply the transition expedient that allows for all reporting periods presented before the date of initial application to exclude disclosure of the amounts of transaction price allocated to the remaining unsatisfied performance obligations. Accordingly, the table below is only for the year ended December 31, 2018.

Changes in deferred revenue related to material right performance obligations were as follows:

	Year Ended December 31, 2018 (in thousands)
Balance, beginning of period	$ 51,624
Deferral of revenue	20,925
Recognition of unearned revenue	(7,898)
Balance, end of period	$ 64,651

We expect to recognize $9.0 million of deferred revenue related to material right performance obligations in 2019 and 2020, and $46.7 million of such deferred revenue thereafter.

Assets Recognized from the Costs to Obtain and Costs to Fulfill Revenue Contracts

We recognize an asset for the incremental costs of obtaining a contract with a client if we expect the amortization period to be longer than one year. We have determined that certain selling and commission costs meet the capitalization criteria under ASC 340-40, which prior to the adoption of ASU 2014-09 were expensed as incurred. We also recognize an asset for the costs to fulfill a contract with a client if such costs are specifically identifiable, generate or enhance resources used to satisfy future performance obligations, and are expected to be recovered. We have determined that substantially all costs related to implementation activities are administrative in nature and also meet the capitalization criteria under ASC 340-40. These capitalized costs to fulfill principally relate to upfront direct costs that are expected to be recovered through margin and that enhance our ability to satisfy future performance obligations.

The assets related to both costs to obtain, and costs to fulfill, contracts with clients are accounted for utilizing a portfolio approach, and are capitalized and amortized over the expected period of benefit, which we have determined to be the estimated client relationship of ten years. The expected period of benefit has been determined to be the estimated life of the client relationship primarily because we incur no new costs to obtain, or costs to fulfill, a contract upon renewal of such contract. Additional commission costs may be incurred when an existing client purchases additional applications; however, these commission costs relate solely to the additional applications purchased and are not related to contract renewal. Furthermore, additional fulfillment costs associated with existing clients purchasing additional applications are minimized by our seamless single-database platform. These assets are presented as deferred contract costs in the accompanying consolidated balance sheets. Amortization expense related to costs to obtain and costs to fulfill a contract are included in the “sales and marketing” and “general and administrative” line items in the accompanying consolidated statements of income.

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The following table presents the asset balance and related amortization expense for these contract costs:

	As of and for the Year Ended December 31, 2018			
	Beginning Balance	Capitalization of Costs	Amortization	Ending Balance
	(in thousands)			
Costs to obtain a contract	$126,207	$ 51,858	$ (19,076)	$158,989
Costs to fulfill a contract	$72,061	$ 41,224	$ (11,529)	$101,756

Cost of Revenues

Our costs and expenses applicable to total revenues represent operating expenses and systems support and technology costs, including labor and related expenses, bank fees, shipping fees and costs of paper stock, envelopes, etc. In addition, costs included to derive gross margins are comprised of support labor and related expenses, related hardware costs and applicable depreciation and amortization costs.

Advertising Costs

Advertising costs are expensed the first time that advertising takes place. Advertising costs for the years ended December 31, 2018, 2017 and 2016 were $16.8 million, $7.9 million and $4.9 million, respectively.

Sales Taxes

We collect and remit sales tax on sales of time and attendance clocks and on payroll services in certain states. These taxes are recognized on a net basis, and therefore, excluded from revenues. For the years ended December 31, 2018, 2017 and 2016, sales taxes collected and remitted were $6.5 million, $5.0 million and $4.3 million, respectively.

Employee Stock-Based Compensation

Time-based stock compensation awards to employees are recognized on a pro-rata basis over the applicable vesting period as compensation costs in the consolidated statements of income based on their fair values measured as of the date of grant. Market-based stock compensation awards to employees are recognized on a pro-rata basis over the applicable estimated vesting period as compensation costs in the consolidated statements of income based on their fair value as of the date of the grant unless vesting occurs sooner at which time the remaining respective unrecognized compensation cost is recognized.

Employee Stock Purchase Plan

An award issued under the Paycom Software, Inc. Employee Stock Purchase Plan (the “ESPP”) is classified as a share-based liability and recognized at the fair value of the award. Expense is recognized, net of estimated forfeitures, on a straight-line basis over the requisite service period.

Income Taxes

Our consolidated financial statements include a provision for income taxes incurred for the anticipated tax consequences of the reported results of operations using the asset and liability method. Under this method, we recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial reporting and tax basis of assets and liabilities, as well as for operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using the tax rates that are expected to apply to taxable income for the years in which those tax assets and liabilities are expected to be realized or settled. We recognize a valuation allowance to reduce our deferred tax assets to the net amount that we believe is more likely than not to be realized.

We file income tax returns in the United States and various state jurisdictions. We evaluate tax positions taken or expected to be taken in the course of preparing our tax returns and disallow the recognition of tax positions not deemed to meet a “more-likely-than-not” threshold of being sustained by the applicable tax authority. We do not believe there are any tax positions taken within the consolidated financial statements that do not meet this threshold. Our policy is to recognize interest and penalties, if any, related to uncertain tax positions as a component of general and administrative expenses. We have one open income tax examination as of December 31, 2018 with the state of Virginia. However, we do not expect the result of the examination to impact income tax expense. We file income tax returns with the United States federal government and various state jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years prior to 2015.

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Seasonality

Our revenues are seasonal in nature. Recurring revenues include revenues relating to the annual processing of payroll forms, such as Form W-2, Form 1099, and Form 1095 and revenues from processing unscheduled payroll runs (such as bonuses) for our clients. Because payroll forms are typically processed in the first quarter of the year, first quarter revenues and margins are generally higher than in subsequent quarters. These seasonal fluctuations in revenues can also have an impact on gross profits. Historical results impacted by these seasonal trends should not be considered a reliable indicator of our future results of operations.

Recently Issued Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." The purpose of this new guidance is to increase the transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet as well as providing additional disclosure requirements related to leasing arrangements. The new guidance is effective for us beginning January 1, 2019, which we plan to adopt using the modified retrospective method and the transition relief guidance provided by the FASB in ASU 2018-11. Under this adoption method, we will not restate comparative prior periods and we will carry forward the assessment of whether our contracts are or contain leases, the classification of our leases and the remaining lease terms. Based on our current portfolio of leases, approximately $21.6 million of lease assets and liabilities will be recognized on our balance sheet upon adoption, primarily relating to operating leases for real estate. Under the transition relief guidance, we have elected the lease vs. non-lease components practical expedient relating to the asset class of real estate, the short-term lease exemption practical expedient and the package of practical expedients. The Company has determined that it will not elect the practical expedient related to hindsight. In connection with the adoption of this standard, the Company is updating its control framework for any new internal controls related to leases that will be required, as well as any changes to existing controls, effective with the January 1, 2019 adoption.

3. PROPERTY AND EQUIPMENT

Property and equipment and accumulated depreciation and amortization were as follows:

	December 31,	
	2018	2017
	(in thousands)	
Property and equipment		
Buildings	$101,421	$60,441
Software and capitalized software costs	66,634	41,996
Computer equipment	39,492	27,928
Rental clocks	16,950	13,131
Furniture, fixtures and equipment	16,474	7,528
Leasehold improvements	1,274	767
Vehicles	74	—
	242,319	151,791

Less: accumulated depreciation and amortization	(82,969)	(53,525)
	159,350	98,266
Construction in progress	8,589	40,446
Land	9,023	8,993
Property and equipment, net	$176,962	$147,705

We capitalize computer software development costs related to software developed for internal use in accordance with ASC 350-40. For the years ended December 31, 2018 and 2017, we capitalized $22.0 million and $15.8 million, respectively, of computer software development costs related to software developed for internal use.

Included in the construction in progress balance at December 31, 2018 and 2017 is $0.1 and $2.0 million in retainage, respectively.

Rental clocks included in property and equipment, net represent time clocks issued to clients under month-to-month operating leases.

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We capitalize interest incurred for indebtedness related to construction in progress. For the years ended December 31, 2018, 2017 and 2016, we incurred costs of $1.6 million, $1.7 million and $1.3 million, respectively. For the years ended December 31, 2018, 2017 and 2016, interest cost of $0.8 million, $0.8 million and $0.4 million, respectively, was capitalized.

Depreciation and amortization expense for property and equipment, net was $29.4 million, $18.5 million and $12.0 million for the years ended December 31, 2018, 2017 and 2016, respectively.

4. GOODWILL AND INTANGIBLE ASSETS, NET

Goodwill represents the excess of acquired cost over our net tangible and identified intangible assets. As of both December 31, 2018 and 2017, goodwill totaled $51.9 million. We have selected June 30 as our annual goodwill impairment testing date. We have elected to perform a qualitative analysis of the fair value of our goodwill and determined there was no impairment as of either June 30, 2018 or 2017. As of December 31, 2018 and 2017, there were no indicators of impairment.

All of our intangible assets other than goodwill are considered to have definite lives and, as such, are subject to amortization. The components of intangible assets are as follows:

	December 31, 2018			
	Weighted Average Remaining Useful Life	Gross	Accumulated Amortization	Net
	(Years)	(dollars in thousands)		
Intangibles:				
Trade name	3.5	$3,194	$ (2,449)	$745
Total		$3,194	$ (2,449)	$745

	December 31, 2017			
	Weighted Average Remaining Useful Life	Gross	Accumulated Amortization	Net
	(Years)	(dollars in thousands)		
Intangibles:				
Trade name	4.5	$3,194	$ (2,236)	$958
Total		$3,194	$ (2,236)	$958

Amortization of intangible assets the years ended December 31, 2018, 2017 and 2016 was $0.2 million, $0.9 million and $1.6 million, respectively.

Estimated amortization expense for our existing intangible assets for the next five years and thereafter is as follows (in thousands):

Year Ending December 31,	Amortization
2019	$ 213
2020	213
2021	213
2022	106
Total	$ 745

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5. LONG-TERM DEBT

Our long-term debt consisted of the following:

	December 31,	
	2018	2017
	(in thousands)	
Net term note to bank due September 7, 2025	$34,389	$35,302
Total long-term debt (including current portion)	34,389	35,302
Less: Current portion	(1,775)	(888)
Total long-term debt, net	$32,614	$34,414

On December 7, 2017, we entered into a senior secured term credit agreement (the “Term Credit Agreement”), pursuant to which JPMorgan Chase Bank N.A., Bank of America, N.A. and Kirkpatrick Bank have agreed to make certain term loans to us (the “Term Loans”) in an aggregate principal amount of $60.0 million on or prior to September 7, 2018 (the “Term Loan Draw Expiration Date”). On September 12, 2018, we entered into the First Amendment to the Term Credit Agreement dated effective as of September 7, 2018, which extended the Term Loan Draw Expiration Date to March 7, 2019. As of December 31, 2018, our indebtedness of $34.6 million consisted solely of Term Loans made under the Term Credit Agreement. Unamortized debt issuance costs of $0.2 million and $0.2 million as of December 31, 2018 and 2017, respectively, are presented as a direct deduction from the carrying amount of the debt liability.

After giving effect to the Term Loans made on December 7, 2017, there was $24.5 million of borrowing capacity remaining under the Term Credit Agreement as of December 31, 2018. Our obligations under the Term Loans are secured by a mortgage and first priority security interest in our headquarters property. Term Loans made after December 7, 2017 may be used to finance hard and soft costs related to the completion of construction of our fourth headquarters building and any landscaping, groundwork, parking lots and roads reasonably incidental thereto. The Term Loans mature on September 7, 2025 and bear interest, at our option, at either (a) a prime rate plus 1.0% or (b) an adjusted LIBOR rate for the interest period in effect for such Term Loan plus 1.5%.

Under the Term Credit Agreement, we are subject to two material financial covenants, which require us to maintain a fixed charge coverage ratio of not less than 1.25 to 1.0 and a funded indebtedness to EBITDA ratio of not greater than 2.0 to 1.0. As of December 31, 2018, we were in compliance with these covenants.

On February 12, 2018, we entered into a senior secured revolving credit agreement (the “Revolving Credit Agreement”) with JPMorgan Chase Bank, N.A. and Bank of America, N.A. that provides for a senior secured revolving credit facility (the “Facility”) in the aggregate principal amount of $50.0 million, which may be increased to up to $100.0 million, subject to obtaining additional lender commitments and certain approvals and satisfying certain other conditions. The Facility includes a $5.0 million sublimit for swingline loans and a $2.5 million sublimit for letters of credit. The Facility is scheduled to mature on February 12, 2020. Borrowings under the Facility will generally bear interest at a prime rate plus 1.0% or, at our option, an adjusted LIBOR rate for the interest period in effect for such borrowing plus 1.5%. The proceeds of the loans and letters of credit under the Facility are to be used only for our general business purposes and working capital. Letters of credit are to be issued only to support our business operations. As of December 31, 2018, we did not have any borrowings outstanding under the Facility.

Under the Revolving Credit Agreement, we are required to maintain a fixed charge coverage ratio of not less than 1.25 to 1.0 and a funded indebtedness to EBITDA ratio of not greater than 2.0 to 1.0. Additionally, the Revolving Credit Agreement contains customary affirmative and negative covenants, including covenants limiting our ability to, among other things, grant liens, incur debt, effect certain mergers, make certain investments, dispose of assets, enter into certain transactions, including swap agreements and sale and leaseback transactions, pay dividends or distributions on our capital stock, and enter into transactions with affiliates, in each case subject to customary exceptions for a facility of the size and type of the Facility. As of December 31, 2018, we were in compliance with all covenants related to the Revolving Credit Agreement.

As of December 31, 2018 and 2017, the carrying value of our total long-term debt approximated its fair value as of such date. The fair value of our long-term debt is estimated based on the borrowing rates currently available to us for bank loans with similar terms and maturities.

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Aggregate future maturities of long-term debt for the next five years and thereafter (including current portion) as of December 31, 2018 are as follows (in thousands):

Year Ending December 31,	
2019	$1,775
2020	1,775
2021	1,775
2022	1,775
2023	1,775
Thereafter	25,738
Total	$34,613

6. DERIVATIVE INSTRUMENTS

In December 2017, we entered into a floating-to-fixed interest rate swap agreement to limit the exposure to floating interest rate risk related to the Term Loans. We do not hold derivative instruments for trading or speculative purposes. The interest rate swap agreement effectively converts a portion of the variable interest rate payments to fixed interest rate payments. We account for our derivatives under ASC Topic 815, “Derivatives and Hedging,” and recognize all derivative instruments on the consolidated balance sheets at fair value as either short-term or long-term assets or liabilities based on their anticipated settlement date. See Note 7, “Fair Value of Financial Instruments”. We have elected not to designate our interest rate swap as a hedge; therefore, changes in the fair value of the derivative instrument are being recognized in our consolidated statements of income within Other income, net.

The objective of the interest rate swap is to reduce the variability in the forecasted interest payments of the Term Loans, which is based on a one-month LIBOR rate versus a fixed interest rate of 2.54% on a notional value of $35.5 million. Under the terms of the interest rate swap agreement, we will receive quarterly variable interest payments based on the LIBOR rate and will pay interest at a fixed rate. The interest rate swap agreement has a maturity date of September 7, 2025. For the years ended December 31, 2018 and 2017, we recognized a gain of $0.7 million and loss of $0.6 million, respectively, for the change in fair value of the interest rate swap, which is included in Other income, net in the consolidated statements of income.

7. FAIR VALUE OF FINANCIAL INSTRUMENTS

Our financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable, funds held for clients, client funds obligation and long-term debt. The carrying amount of cash and cash equivalents, accounts receivable, accounts payable, funds held for clients and client fund obligation approximates fair value because of the short-term nature of the instruments. See Note 5 for discussion of the fair value of our debt.

As discussed in Note 2, we invest the funds held for clients in money market funds, demand deposit accounts, commercial paper with a maturity duration less than three months and certificates of deposit, and classify as cash and cash equivalents within the funds held for clients line item in the consolidated balance sheets. Short-term investments in commercial paper and certificates of deposit with a maturity duration greater than three months are classified as available-for-sale securities, and are also included within the funds held for clients line item. These available-for-sale securities are recorded on the balance sheet at fair value, which approximates the amortized cost of the securities. As of December 31, 2018 and 2017, all available-for-sale securities and certificates of deposit were due in one year or less.

As discussed in Note 6, during the year ended December 31, 2017, we entered into an interest rate swap. The interest rate swap is measured on a recurring basis based on quoted prices for similar financial instruments and other observable inputs recognized at fair value.

The accounting standard for fair value measurements establishes a three-level fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

- Level 1 – Observable inputs such as quoted prices in active markets
- Level 2 – Inputs other than quoted prices in active markets for identical assets or liabilities that are observable either directly or indirectly or quoted prices that are not active
- Level 3 – Unobservable inputs in which there is little or no market data

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Included in the following table are the Company's major categories of assets and liabilities measured at fair value on a recurring basis as of December 31, 2018 and 2017:

	December 31, 2018			
	Level 1	Level 2	Level 3	Total
Assets:	(in thousands)			
Commercial paper	$—	$21,041	$ —	$21,041
Certificates of deposit	$—	$6,000	$ —	$6,000
Interest rate swap	$—	$17	$ —	$17

	December 31, 2017			
	Level 1	Level 2	Level 3	Total
Assets:	(in thousands)			
Commercial paper	$—	$14,918	$ —	$14,918
Certificates of deposit	$—	$21,500	$ —	$21,500
Liabilities:				
Interest rate swap	$—	$649	$ —	$649

8. EMPLOYEE SAVINGS PLAN AND EMPLOYEE STOCK PURCHASE PLAN

Employees over the age of 18 and have completed ninety days of service are eligible to participate in our 401(k) plan. We have made a Qualified Automatic Contribution Arrangement ("QACA") election, whereby the Company matches the contribution of our employees equal to 100% of the first 1% of salary deferrals and 50% of salary deferrals between 2% and 6%, up to a maximum matching contribution of 3.5% of an employee's salary each plan year. We are allowed to make additional discretionary matching contributions and discretionary profit sharing contributions. Employees are 100% vested in amounts attributable to salary deferrals and rollover contributions. The QACA matching contributions as well as the discretionary matching and profit sharing contributions vest 100% after two years of employment from the date of hire. Matching contributions amounted to $5.3 million, $4.1 and $3.5 million for the years ended December 31, 2018, 2017 and 2016, respectively.

The ESPP has overlapping offering periods, with each offering period lasting approximately 24 months. At the beginning of each offering period, eligible employees may elect to contribute, through payroll deductions, up to 10% of their compensation, subject to an annual per employee maximum. Eligible employees purchase shares of the Company's common stock at a price equal to 85% of the fair market value of the shares on the exercise date. The maximum number of shares that may be purchased by a participant during each offering period is 2,000 shares, subject to limits specified by the Internal Revenue Service. The shares reserved for purposes of the ESPP are shares the Company purchases in the open market. The maximum aggregate number of shares of the Company's common stock that may be purchased by all participants under the ESPP is 2,000,000 shares. During the years ended December 31, 2018, 2017 and 2016, eligible employees purchased 59,041, 76,728 and 110,658 shares, respectively, of the Company's common stock under the ESPP. Compensation expense related to the ESPP is recognized on a straight-line basis over the requisite service period. Our compensation expense related to the ESPP was $1.3 million, $0.8 million and $0.6 million for the years ended December 31, 2018, 2017 and 2016, respectively.

9. EARNINGS PER SHARE

Basic earnings per share is based on the weighted average number of shares of common stock outstanding for the period. Diluted earnings per share is computed in a similar manner to basic earnings per share after assuming the issuance of shares of common stock for all potentially dilutive shares of restricted stock whether or not they are vested.

In accordance with ASC Topic 260, “Earnings Per Share,” the two-class method determines earnings for each class of common stock and participating securities according to an earnings allocation formula that adjusts the income available to common stockholders for dividends or dividend equivalents and participation rights in undistributed earnings. Certain unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and, therefore, are included in computing earnings per share pursuant to the two-class method. The unvested shares of restricted stock granted in 2015 are considered participating securities, while all other unvested shares of restricted stock are not considered participating securities.

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The following is a reconciliation of net income and the shares of common stock used in the computation of basic and diluted earnings per share (in thousands, except share and per share amounts):

	Year Ended December 31,		
	2018	2017 *As Adjusted	2016 *As Adjusted
Numerator:			
Net income	$137,065	$123,486	$70,421
Less: income allocable to participating securities	(159)	(315)	(535)
Income allocable to common shares	$136,906	$123,171	$69,886
Add back: undistributed earnings allocable to participating securities	159	315	535
Less: undistributed earnings reallocated to participating securities	(156)	(310)	(535)
Numerator for diluted earnings per share	$136,909	$123,176	$69,886
Denominator:			
Basic weighted average shares outstanding	57,711,315	57,839,155	57,550,204
Dilutive effect of unvested restricted stock	871,171	950,864	1,417,895
Diluted weighted average shares outstanding	58,582,486	58,790,019	58,968,099
Earnings per share:			
Basic	$2.37	$2.13	$1.21
Diluted	$2.34	$2.10	$1.19

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

10. STOCKHOLDERS' EQUITY AND STOCK-BASED COMPENSATION

We have historically issued shares of restricted stock under the Paycom Software, Inc. 2014 Long-Term Incentive Plan (the "LTIP") that are subject to either time-based vesting conditions or market-based vesting conditions. The market-based vesting conditions are based on the Company's total enterprise value ("TEV") exceeding certain specified thresholds. Compensation expense related to the issuance of shares with time-based vesting conditions ("Time-Based Shares") is measured based on the fair value of the award on the grant date and recognized over the requisite service period on a straight-line basis. Compensation expense related to the issuance of shares with market-based vesting conditions ("Market-Based Shares") is measured based upon the fair value of the award on the grant date and recognized on a straight-line basis over the vesting period based upon the probability that the vesting condition will be met.

The following table presents a summary of the grant-date fair values of restricted stock granted during the years ended December 31, 2018, 2017 and 2016 and the related assumptions:

	Year Ended December 31,		
	2018	2017	2016
Grant-date fair value of restricted stock	$81.14 - $122.83	$46.78 - $60.67	$23.15 - $49.34
Risk-free interest rate	2.54%	1.85%	1.28% - 1.36%
Estimated volatility	25.0%	23.0%	21.0% - 23.0%
Expected life (in years)	2.0	2.3	2.7

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

	Time-Based Shares		Market-Based Shares	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Unvested shares of restricted stock outstanding at December 31, 2017	888,680	$ 42.17	—	$ —
Granted	337,050	99.76	284,118	82.84
Vested	(314,224)	34.14	(283,080)	82.84
Forfeited	(105,037)	56.26	(1,038)	82.64
Unvested shares of restricted stock outstanding at December 31, 2018	806,469	$ 67.54	—	$ —

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During the year ended December 31, 2018, we issued an aggregate of 621,168 shares of restricted stock to our executive officers, certain non-executive employees and non-employee directors under the LTIP, consisting of 284,118 Market-Based Shares and 337,050 Time-Based Shares. The Market-Based Shares were scheduled to vest 50% on the first date that the Company's TEV (calculated as defined in the applicable restricted stock award agreement) equaled or exceeded $5.9 billion and 50% on the first date that the Company's TEV equaled or exceeded $6.2 billion, in each case provided that (i) such date occurred on or before the sixth anniversary of the grant date and (ii) the recipient was employed by, or providing services to, the Company or a subsidiary on the applicable vesting date. As shown in the table below, all Market-Based Shares issued on January 26, 2018 vested during the year ended December 31, 2018.

The following table summarizes vesting activity for Market-Based Shares during the year ended December 31, 2018, the associated compensation cost recognized in connection with the vesting event and the number of shares withheld to satisfy tax withholding obligations:

Vesting Condition	Date Vested	Number of Shares Vested	Compensation Cost Recognized Upon Vesting	Shares Withheld for Taxes[1]
Market-based (TEV = $5.9 billion)	March 14, 2018	141,599	$9.7 million	54,000
Market-based (TEV = $6.2 billion)	March 23, 2018	141,481	$10.1 million	54,909

[1] All shares withheld to satisfy tax withholding obligations are held as treasury stock.

The vesting conditions for Time-Based Shares issued in 2018 vary based on the category of the recipient. The Time-Based Shares issued to executive officers and non-executive sales employees in 2018 will vest in three equal annual tranches beginning on a specified initial vesting date and thereafter on the first and second anniversaries of such date, provided that the executive officer or non-executive sales employee is employed by, or providing services to, the Company on the applicable vesting date. Time-Based Shares issued to certain non-executive, non-sales employees during 2018 will vest 25% on a specified initial vesting date and 25% on each of the first three anniversaries of such initial vesting date, provided that the recipient is employed by, or providing services to, the Company on the applicable vesting date. Time-based shares issued to non-employee members of our Board of Directors will cliff-vest on the seventh day following the first anniversary of the date of grant, provided that such director is providing services to the Company through the applicable vesting date.

Our total compensation expense related to restricted stock was $36.4 million, $36.0 million and $20.8 million for the years ended December 31, 2018, 2017 and 2016, respectively. There was $41.4 million of unrecognized compensation cost, net of estimated forfeitures, related to unvested shares of restricted stock outstanding as of December 31, 2018. The unrecognized compensation cost is expected to be recognized over a weighted average period of 1.8 years as of December 31, 2018.

We capitalized stock-based compensation costs related to software developed for internal use of $3.7 million, $3.3 million and $1.8 million for the years ended December 31, 2018, 2017 and 2016, respectively.

The following table presents non-cash stock-based compensation expense resulting from restricted stock awards, which is included in the following line items in the accompanying consolidated statements of income for the years ended December 31, 2018, 2017 and 2016:

	Year Ended December 31,		
	2018	2017 *As Adjusted	2016 *As Adjusted
	(in thousands)		
Operating expense	$4,041	$ 3,950	$ 2,217
Sales and marketing	7,510	5,023	3,028
Research and development	3,013	1,912	836
General and administrative	21,847	25,162	14,715
Total non-cash stock-based compensation expense	$36,411	$ 36,047	$ 20,796

11. RELATED-PARTY TRANSACTIONS

Our Chief Sales Officer owned a .01% general partnership interest and a 10.49% limited partnership interest in 417 Oakbend, LP, a Texas limited partnership, until April 2016. For the period under his ownership during 2016, we paid rent on our Dallas office space to 417 Oakbend, LP in the amount of $0.1 million.

Paycom Software, Inc.

Notes to the Consolidated Financial Statements

12. COMMITMENTS AND CONTINGENCIES

Employment Agreements

We have employment agreements with certain of our executive officers. The agreements allow for annual compensation, participation in executive benefit plans, and performance-based cash bonuses.

Incentive Plan

On May 2, 2016, our stockholders approved the Paycom Software, Inc. Annual Incentive Plan (the "Incentive Plan"). The Incentive Plan provides for payment of incentive compensation that is not subject to certain federal income tax deduction limitations. Participation in the Incentive Plan is limited to certain of our employees designated by the Compensation Committee of the Board of Directors.

Operating Leases and Deferred Rent

Our leases primarily consist of several noncancellable operating leases for office space with contractual terms expiring from 2019 to 2024. Minimum rent expenses are recognized over the lease term. The lease term is defined as the fixed noncancellable term of the lease plus all periods, if any, for which failure to renew the lease imposes a penalty on the Company in an amount that a renewal appears, at the inception of the lease, to be reasonably assured. When a lease contains a predetermined fixed escalation of the minimum rent, we recognize the related rent expense on a straight-line basis and record the difference between the recognized rent expense and the amount payable under the lease as a liability. We had $1.4 million and $1.3 million as of December 31, 2018 and 2017, respectively, recognized as a liability for deferred rent.

Future annual minimum lease payments under noncancellable operating leases with initial or remaining terms of one year or more as of December 31, 2018 were as follows (in thousands):

Year Ending December 31,	
2019	$8,315
2020	6,900
2021	5,224
2022	4,478
2023	2,839
Thereafter	502
Total minimum lease payments	$28,258

Rent expense under operating leases for the years ended December 31, 2018, 2017 and 2016 was $7.6 million, $6.1 million and $5.6 million, respectively.

Legal Proceedings

We are involved in various legal proceedings in the ordinary course of business. Although we cannot predict the outcome of these proceedings, legal matters are subject to inherent uncertainties and there exists the possibility that the ultimate resolution of these matters could have a material adverse effect on our business, financial condition, results of operations and cash flows.

Paycom Software, Inc.

Notes to the Consolidated Financial Statements

13. INCOME TAXES

The items comprising income tax expense are as follows:

	Year Ended December 31, 2018	2017 *As Adjusted	2016 *As Adjusted
	(in thousands)		
Provision for current income taxes			
Federal	$12,414	$10,136	$12,207
State	4,155	1,791	3,044
Total provision for current income taxes	16,569	11,927	15,251
Provision (benefit) for deferred income taxes, net			
Federal	14,365	(3,865)	12,708
State	6,712	(3,816)	2,632
Total benefit for deferred income taxes, net	21,077	(7,681)	15,340
Total provision for income taxes	$37,646	$4,246	$30,591

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

The following schedule reconciles the statutory Federal tax rate to the effective income tax rate:

	Year Ended December 31, 2018	2017 *As Adjusted	2016 *As Adjusted
Federal statutory tax rate	21%	35%	35%
Increase (decrease) resulting from:			
State income taxes, net of Federal income tax benefit	6%	4%	4%
Nondeductible expenses	1%	0%	0%
Research credit, Federal benefit	(2%)	(2%)	(1%)
Section 199 - Qualified production activities	0%	(1%)	(1%)
Stock-based compensation	(4%)	(13%)	(7%)
Remeasurement of deferred tax liabilities	0%	(20%)	0%
Effective income tax rate	22%	3%	30%

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

Our effective income tax rate was 22% and 3% for the years ended December 31, 2018 and 2017, respectively. The lower effective income tax rate for the year ended December 31, 2017 primarily resulted from the remeasurement of our deferred tax balance due to the Tax Act and the reduction in the excess tax benefits recognized related to stock-based compensation.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The significant components of our deferred tax assets and liabilities were as follows:

	December 31,	
	2018	2017 *As Adjusted
	(in thousands)	
Deferred income tax assets (liabilities):		
Stock-based compensation	$1,529	$945
Investment in Paycom Payroll Holdings, LLC	(73,020)	(51,821)
Net operating losses	935	1,677
Federal tax credits	350	70
Noncurrent deferred income tax liabilities, net	$(70,206)	$(49,129)

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

Paycom Software, Inc.

Notes to the Consolidated Financial Statements

At December 31, 2018, we had net operating loss carryforwards for state income tax purposes of approximately $0.9 million which are available to offset future state taxable income that begin expiring in 2030.

At December 31, 2018 and 2017, we had no material unrecognized tax benefits related to uncertain tax positions.

We file income tax returns with the United States federal government and various state jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years prior to 2015.

14. SELECTED QUARTERLY FINANCIAL DATA (unaudited)

The following tables set forth selected quarterly statements of income data for the periods indicated (in thousands, except share and per share amounts):

	Quarter Ended			
	March 31, 2018	June 30, 2018	September 30, 2018	December 31, 2018
Revenues	$153,916	$128,800	$133,288	$150,332
Operating income	$51,020	$43,037	$36,245	$43,413
Net income	$41,160	$35,722	$28,769	$31,414
Earnings per share, basic	$0.71	$0.62	$0.50	$0.55
Earnings per share, diluted	$0.70	$0.61	$0.49	$0.54
Weighted average shares outstanding:				
Basic	57,793,023	57,837,312	57,726,790	57,491,280
Diluted	58,738,732	58,720,785	58,545,061	58,238,231

	Quarter Ended			
	March 31, 2017	June 30, 2017	September 30, 2017	December 31, 2017
	*As Adjusted	*As Adjusted	*As Adjusted	*As Adjusted
Revenues	$119,508	$98,227	$101,287	$114,025
Operating income	$52,510	$18,792	$22,007	$36,401
Net income	$33,694	$20,016	$20,910	$48,866
Earnings per share, basic	$0.58	$0.34	$0.36	$0.84
Earnings per share, diluted	$0.57	$0.34	$0.35	$0.83

Weighted average shares outstanding:				
Basic	57,307,187	57,898,914	58,003,222	58,100,141
Diluted	58,525,980	58,816,442	58,873,502	58,850,271

* Prior year amounts have been recast to reflect the adoption of ASU 2014-09. See Note 2 for description of adjustments.

15. SUBSEQUENT EVENTS

On January 17, 2019, we issued an aggregate of 512,069 restricted shares of common stock to our executive officers, certain non-executive, non-sales employees and non-executive sales management employees under the LTIP, consisting of 280,960 Market-Based Shares and 231,109 Time-Based Shares. Market-Based Shares will vest 50% on the first date that the Company's TEV (calculated as defined in the applicable restricted stock award agreement) equals or exceeds $8.65 billion and 50% on the first date that the Company's TEV equals or exceeds $9.35 billion, in each case provided that (i) such date occurs on or before the sixth anniversary of the grant date and (ii) the recipient is employed by, or providing services to, the Company on the applicable vesting date. Time-Based Shares granted to non-executive employees will vest 25% on a specified initial vesting date and 25% on each of the first three anniversaries of such initial vesting date, provided that the recipient is employed by, or providing services to, the Company or a subsidiary on the applicable vesting date. Time-Based Shares granted to executive officers and sales management employees will vest in three equal annual tranches beginning on a specified initial vesting date and thereafter on the first and second anniversaries of such date, provided that the executive officer or sales management employee is employed by, or providing services to, the Company on the applicable vesting date. On February 13, 2019, the Company recognized $14.9 million of compensation cost in connection with the vesting of 140,218 of the Market-Based Shares issued on January 17, 2019.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure
None.

Item 9A. Controls and Procedures
Evaluation of Disclosure Controls and Procedures

The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, refers to controls and procedures that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that such information is accumulated and communicated to a company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. We believe, however, that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving desired control objectives, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud or error within a company, if any, have been detected.

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

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our management, under the supervision and with the participation of our chief executive officer and chief financial officer, assessed the effectiveness of our internal control over financial reporting based on criteria established in the 2013 Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, management concluded that our internal control over financial reporting was effective as of December 31, 2018.

The effectiveness of our internal control over financial reporting as of December 31, 2018 has been audited by Grant Thornton LLP, an independent registered public accounting firm, as stated in its report included below.

Changes in Internal Control Over Financial Reporting

In connection with the Company's adoption of ASU No. 2016-02, "Leases (Topic 842)," the Company is updating its control framework for any new internal controls related to lease liabilities that will be required, as well as any changes to existing controls, effective with the January 1, 2019 adoption.

There have been no material changes in our internal control over financial reporting that occurred during the quarter ended December 31, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information
As previously disclosed, the Company maintains the Paycom Software, Inc. Annual Incentive Plan (the "Annual Incentive Plan"), pursuant to which the Company may grant incentive compensation to certain employees designated by the Compensation Committee of the Board of Directors (the "Compensation Committee"). Awards under the Annual Incentive Plan are made based upon the achievement of performance goals (consisting of individual performance

goals, business unit performance goals or Company performance goals) relating to one or more performance criteria listed in the Annual Incentive Plan, including revenues, earnings per share, and adjusted EBITDA, among others. On February 13, 2019, the Compensation Committee approved an amendment to the Annual Incentive Plan (the “Incentive Plan Amendment”) to add the metric “annual revenue retention rate” to the list of performance criteria, such that future awards under the Annual Incentive Plan may be made subject to the attainment of performance goals relating to annual revenue retention rate. The foregoing description of the Incentive Plan Amendment is qualified in its entirety by reference to the full text of the Incentive Plan Amendment, which is filed as Exhibit 10.6.1 to this Form 10-K and is incorporated herein by reference.

Independent Registered Public Accounting Firm's Report on Internal Control over Financial Reporting

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders

Paycom Software, Inc.

Opinion on internal control over financial reporting

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

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the consolidated financial statements of the Company as of and for the year ended December 31, 2018, and our report dated February 14, 2019 expressed an unqualified opinion on those financial statements.

Basis for opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

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

Definition and limitations of internal control over financial reporting

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

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

/s/ GRANT THORNTON LLP

Oklahoma City, Oklahoma

February 14, 2019

Item 10. Directors, Executive Officers and Corporate Governance

The information required in response to this Item 10 is incorporated herein by reference to our Definitive Proxy Statement to be filed with the SEC pursuant to Regulation 14A of the Exchange Act not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

Item 11. Executive Compensation

The information required in response to this Item 11 is incorporated herein by reference to our Definitive Proxy Statement to be filed with the SEC pursuant to Regulation 14A of the Exchange Act not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required in response to this Item 12 is incorporated herein by reference to our Definitive Proxy Statement to be filed with the SEC pursuant to Regulation 14A of the Exchange Act not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required in response to this Item 13 is incorporated herein by reference to our Definitive Proxy Statement to be filed with the SEC pursuant to Regulation 14A of the Exchange Act not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

Item 14. Principal Accounting Fees and Services

The information required in response to this Item 14 is incorporated herein by reference to our Definitive Proxy Statement to be filed with the SEC pursuant to Regulation 14A of the Exchange Act not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

Item 15. Exhibits, Financial Statement Schedules

(a) Documents filed as part of this Form 10-K

(1) Consolidated Financial Statements: The following consolidated financial statements of Paycom Software, Inc., together with the report thereon, of Grant Thornton LLP, our Independent Registered Public Accounting Firm, are included in Part II, Item 8 of this Form 10-K:

Consolidated Balance Sheets as of December 31, 2018 and 2017

Consolidated Statements of Income, Years Ended December 31, 2018, 2017 and 2016

Consolidated Statements of Stockholders' Equity, Years Ended December 31, 2018, 2017 and 2016

Consolidated Statements of Cash Flows, Years Ended December 31, 2018, 2017 and 2016

Notes to Consolidated Financial Statements

(2) Financial Statement Schedules: Financial statement schedules have been omitted as information required is inapplicable or the information is presented in the consolidated financial statements and the related notes.

(3) Exhibits:

The following exhibits are included herein or incorporated herein by reference:

Exhibit No.	Description
3.1	Amended and Restated Certificate of Incorporation of Paycom Software, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Amendment No. 1 to the Registration Statement on Form S-1/a dated March 31, 2014, filed with the SEC on March 31, 2014).
3.2	Amended and Restated Bylaws of Paycom Software, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015, filed with the SEC on November 6, 2015).
4.1	Form of Common Stock Certificate (incorporated by reference to Exhibit 4.1 to the Company's Amendment No. 1 to the Registration Statement on Form S-1/A dated March 31, 2014, filed with the SEC on March 31, 2014).
4.2	Registration Rights Agreement (incorporated by reference to Exhibit 4.3 to the Company's Registration Statement on Form S-1 dated March 10, 2014, filed with the SEC on March 10, 2014).
4.3	Joinder to Registration Rights Agreement, by and among Paycom Software, Inc. and each of the signatories thereto, dated as of March 6, 2015 (incorporated by reference to Exhibit 4.6 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2015, filed with the SEC on May 13, 2015).
4.4	Amendment No. 1 to the Registration Rights Agreement, by and among Paycom Software, Inc. and each of the signatories thereto, dated as of May 13, 2015 (incorporated by reference to Exhibit 4.7 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, filed with the SEC on August 7, 2015).

4.5	Joinder to Registration Rights Agreement, by and between Paycom Software, Inc. and the Mackesy Family Foundation, dated as of May 27, 2015 (incorporated by reference to Exhibit 4.9 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015, filed with the SEC on November 6, 2015).
4.6	Joinder to Registration Rights Agreement, by and between Paycom Software, Inc. and Anthony & Christie de Nicola Foundation, dated as of August 13, 2015 (incorporated by reference to Exhibit 4.11 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015, filed with the SEC on November 6, 2015).
4.7	Amendment No. 2 to Registration Rights Agreement, by and between Paycom Software, Inc. and each of the signatories thereto, dated as of September 15, 2015 (incorporated by reference to Exhibit 4.12 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015, filed with the SEC on November 6, 2015).
4.8	Joinder to Registration Rights Agreement, by and between Paycom Software, Inc. and The Swani Family Foundation, dated as of October 13, 2015 (incorporated by reference to Exhibit 4.14 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015, filed with the SEC on November 6, 2015).
4.9	Joinder to Registration Rights Agreement, by and between Paycom Software, Inc. and Paul & Anne-Marie Queally Family Foundation, dated as of October 13, 2015 (incorporated by reference to Exhibit 4.16 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015, filed with the SEC on November 6, 2015).

4.10	Joinder to Registration Rights Agreement, by and between Paycom Software, Inc. and Scully Family Charitable Foundation, dated as of December 2, 2015 (incorporated by reference to Exhibit 4.18 to the Company's Annual Report on Form 10-K for the year ended December 31, 2015, filed with the SEC on February 22, 2016).
10.1+	Form of Indemnification Agreement between Paycom Software, Inc. and each of its directors and executive officers (incorporated by reference to Exhibit 10.1 to the Company's Registration Statement on Form S-1 dated March 10, 2014, filed with the SEC on March 10, 2014).
10.2+	Paycom Software, Inc. 2014 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.2 to the Company's Registration Statement on Form S-1 dated March 10, 2014, filed with the SEC on March 10, 2014).
10.2.1+	First Amendment to the Paycom Software, Inc. 2014 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated May 1, 2017, filed with the SEC on May 4, 2017).
10.2.2+	Form of Time and Market-Based Vesting Restricted Stock Award Agreement (CEO) under the Paycom Software, Inc. 2014 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated April 26, 2017, filed with the SEC on April 27, 2017).
10.2.3+	Form of Time and Market-Based Vesting Restricted Stock Award Agreement (Executive) under the Paycom Software, Inc. 2014 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K dated April 26, 2017, filed with the SEC on April 27, 2017).
10.2.4+	Form of Time and Market-Based Vesting Restricted Stock Award Agreement under the Paycom Software, Inc. 2014 Long-Term Incentive Plan (incorporated by reference to Exhibit 99.5 to the Company's Registration Statement on Form S-8, dated January 15, 2019, filed with the SEC on January 15, 2019).
10.2.5+	Form of Time-Based Vesting Restricted Stock Award Agreement under the Paycom Software, Inc. 2014 Long-Term Incentive Plan (incorporated by reference to Exhibit 99.6 to the Company's Registration Statement on Form S-8, dated January 15, 2019, filed with the SEC on January 15, 2019).
10.3+	Executive Employment Agreement by and between Paycom Payroll Holdings, LLC and Chad Richison, dated December 30, 2013 (incorporated by reference to Exhibit 10.4 to the Company's Registration Statement on Form S-1 dated March 10, 2014, filed with the SEC on March 10, 2014).
10.4+	Executive Employment Agreement by and between Paycom Payroll Holdings, LLC and Craig E. Boelte, dated December 30, 2013 (incorporated by reference to Exhibit 10.5 to the Company's Registration Statement on Form S-1 dated March 10, 2014, filed with the SEC on March 10, 2014).
10.5+	Executive Employment Agreement by and between Paycom Payroll Holdings, LLC and Jeffrey D. York, dated December 30, 2013 (incorporated by reference to Exhibit 10.6 to the Company's Registration Statement on Form S-1 dated March 10, 2014, filed with the SEC on March 10, 2014).
10.6+	Paycom Software, Inc. Annual Incentive Plan (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K dated May 5, 2015, filed with the SEC on May 8, 2015).
10.6.1+*	First Amendment to Paycom Software, Inc. Annual Incentive Plan.

10.7	Paycom Software, Inc. Employee Stock Purchase Plan (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated May 5, 2015, filed with the SEC on May 8, 2015).
10.8	Term Credit Agreement, dated December 7, 2017, by and among Paycom Payroll, LLC as the borrower, Paycom Software, Inc. and certain of its subsidiaries as the guarantors, the lenders parties thereto and JPMorgan Chase Bank, N.A. as administrative agent (incorporated by reference to Exhibit 10.12 to the Company's Annual Report on Form 10-K for the year ended December 31, 2017, filed with the SEC on February 14, 2018).
10.8.1	First Amendment to Credit Agreement and Loan Parties' Consent, dated effective as of September 7, 2018, by and among Paycom Payroll, LLC as the borrower, Paycom Software, Inc. and certain of its subsidiaries as the guarantors, the lenders parties thereto and JPMorgan Chase Bank, N.A. as administrative agent (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2018, filed with the SEC on November 1, 2018).

10.9	Real Estate Mortgage, Security Agreement, Assignment of Leases and Rents, Financing Statement and Fixture Filing, dated December 7, 2017, by Paycom Payroll, LLC in favor of JPMorgan Chase Bank, N.A (incorporated by reference to Exhibit 10.13 to the Company's Annual report on Form 10-K for the year ended December 31, 2017, filed with the SEC on February 14, 2018).
10.10	Senior Secured Revolving Credit Agreement, dated February 12, 2018, by and among Paycom Payroll, LLC as the borrower, Paycom Software Inc. and certain of its subsidiaries as the guarantors, the lenders parties thereto and JP Morgan Chase Bank, N.A. as administrative agent (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2018, filed with the SEC on May 5, 2018).
21.1*	List of subsidiaries of the Company
23.1*	Consent of Independent Registered Public Accounting Firm
31.1*	Certification of the Chief Executive Officer of the Company, pursuant to the Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of the Chief Financial Officer of the Company, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1**	Certification of the Chief Executive Officer and Chief Financial Officer of the Company, 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

+ Management contract or compensatory plan or arrangement.

* Filed herewith.

** The certifications attached as Exhibit 32.1 are not deemed "filed" with the SEC and are not to be incorporated by reference into any filing of Paycom Software, Inc. under the Securities Act or the Exchange Act, whether made before or after the date of this Annual Report on Form 10-K, irrespective of any general incorporation language contained in such filing.

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.

Date: February 14, 2019

PAYCOM SOFTWARE, INC.

By: /s/ Chad Richison
Chad Richison
President and Chief Executive Officer
(Principal Executive Officer and duly authorized officer)

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

Date: February 14, 2019

/s/ Chad Richison
Chad Richison
President, Chief Executive Officer and Chairman of the Board of Directors

(Principal Executive Officer)

/s/ Craig E. Boelte
Craig E. Boelte
Chief Financial Officer

(Principal Accounting Officer and Principal Financial Officer)

/s/ Jason D. Clark
Jason D. Clark

Director

/s/ Henry C. Duques
Henry C. Duques

Director

/s/ Janet Haugen
Janet Haugen

Director

/s/ Robert J. Levenson
Robert J. Levenson

Director

/s/ Frederick C. Peters II
Frederick C. Peters II

Director

/s/ J.C. Watts, Jr.
J.C. Watts, Jr.

Director