Pandora Media, Inc.
Form 10-Q
August 01, 2017
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us-gaap:ResearchAndDevelopmentExpenseMember 2017-01-01 2017-06-30 0001230276
p:ServiceAndProcessingCostsMember 2017-04-01 2017-06-30 0001230276
us-gaap:SellingAndMarketingExpenseMember 2017-01-01 2017-06-30 0001230276
us-gaap:SellingAndMarketingExpenseMember 2016-04-01 2016-06-30 0001230276

us-gaap:GeneralAndAdministrativeExpenseMember 2017-01-01 2017-06-30 0001230276
us-gaap:ResearchAndDevelopmentExpenseMember 2016-01-01 2016-06-30 0001230276
us-gaap:CostOfSalesMember 2017-04-01 2017-06-30 0001230276
us-gaap:GeneralAndAdministrativeExpenseMember 2017-04-01 2017-06-30 0001230276
us-gaap:CostOfSalesMember 2016-01-01 2016-06-30 0001230276 us-gaap:SellingAndMarketingExpenseMember
2017-04-01 2017-06-30 0001230276 us-gaap:SellingAndMarketingExpenseMember 2016-01-01 2016-06-30
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us-gaap:ResearchAndDevelopmentExpenseMember 2017-04-01 2017-06-30 0001230276
us-gaap:GeneralAndAdministrativeExpenseMember 2016-01-01 2016-06-30 0001230276
p:ServiceAndProcessingCostsMember 2016-04-01 2016-06-30 0001230276 us-gaap:CostOfSalesMember 2017-01-01
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us-gaap:EmployeeStockMember p:BlackScholesOptionsPricingModelMember 2016-04-01 2016-06-30 0001230276
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us-gaap:PerformanceSharesMember us-gaap:ShareBasedCompensationAwardTrancheOneMember 2016-04-01
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2017-06-30 0001230276 us-gaap:EmployeeSeveranceMember 2017-01-01 2017-06-30 0001230276
us-gaap:SeriesAPreferredStockMember 2017-06-09 0001230276 us-gaap:PerformanceSharesMember 2016-01-01
2016-06-30 0001230276 us-gaap:EmployeeStockMember 2017-01-01 2017-06-30 0001230276
us-gaap:RestrictedStockUnitsRSUMember 2016-01-01 2016-06-30 0001230276
p:EmployeeAndNonEmployeeStockOptionsMember 2016-01-01 2016-06-30 0001230276
us-gaap:PerformanceSharesMember 2017-01-01 2017-06-30 0001230276 us-gaap:RestrictedStockUnitsRSUMember
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Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2017

or

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

For the transition period from to

Commission File Number: 001-35198

Pandora Media, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**94-3352630**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2101 Webster Street, Suite 1650 Oakland, CA	**94612**
(Address of principal executive offices)	(Zip Code)

(510) 451-4100
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted to its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

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. o

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

The number of shares of registrant’s common stock outstanding as of July 27, 2017 was: 242,621,114.

Table of Contents

Pandora Media, Inc.

FORM 10-Q Quarterly Report

Table of Contents

		Page No.
	PART I. FINANCIAL INFORMATION	
Item 1.	Financial Statements (unaudited)	3
	Condensed Consolidated Balance Sheets as of December 31, 2016 and June 30, 2017	3
	Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2016 and 2017	4
	Condensed Consolidated Statements of Comprehensive Loss for the Three and Six Months Ended June 30, 2016 and 2017	5
	Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2016 and 2017	6
	Notes to Condensed Consolidated Financial Statements	7
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	27
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	44
Item 4.	Controls and Procedures	45
	PART II. OTHER INFORMATION	
Item 1.	Legal Proceedings	46
Item 1A.	Risk Factors	46
Item 6.	Exhibits	71
	Signatures	73

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Pandora Media, Inc.
Condensed Consolidated Balance Sheets
(in thousands, except share and per share amounts) (unaudited)

	As of December 31, 2016	As of June 30, 2017
Assets		
Current assets		
Cash and cash equivalents	$ 199,944	$ 209,581
Short-term investments	37,109	18,056
Accounts receivable, net of allowance of $3,633 at December 31, 2016 and $5,708 at June 30, 2017	309,267	288,347
Prepaid content acquisition costs	46,310	39,869
Prepaid expenses and other current assets	33,191	18,188
Assets held for sale	—	227,844
Total current assets	625,821	801,885
Long-term investments	6,252	—
Property and equipment, net	124,088	120,792
Goodwill	306,691	71,243
Intangible assets, net	90,425	23,235
Other long-term assets	31,533	13,490
Total assets	$ 1,184,810	$ 1,030,645
Liabilities, redeemable convertible preferred stock and stockholders' equity		
Current liabilities		
Accounts payable	$ 15,224	$ 12,780
Accrued liabilities	35,465	43,601
Accrued content acquisition costs	93,723	88,260
Accrued compensation	60,353	45,580
Deferred revenue	28,359	32,475
Other current liabilities	20,993	—
Liabilities held for sale	—	43,059
Total current liabilities	254,117	265,755
Long-term debt, net	342,247	352,157
Other long-term liabilities	34,187	25,701
Total liabilities	630,551	643,613
Redeemable convertible preferred stock: 172,500 shares issued and outstanding at June 30, 2017	—	173,095
Stockholders' equity		
Common stock: 235,162,757 shares issued and outstanding at December 31, 2016 and 242,412,275 at June 30, 2017	24	24
Additional paid-in capital	1,264,693	1,347,285
Accumulated deficit	(709,636)	(1,132,721)
Accumulated other comprehensive loss	(822)	(651)
Total stockholders' equity	554,259	213,937
Total liabilities, redeemable convertible preferred stock and stockholders' equity	$ 1,184,810	$ 1,030,645

The accompanying notes are an integral part of the condensed consolidated financial statements.

Table of Contents

Pandora Media, Inc.
Condensed Consolidated Statements of Operations
(in thousands, except per share amounts)
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2016	**2017**	**2016**	**2017**
Revenue				
Advertising	$265,126	$278,204	$485,434	$501,512
Subscription and other	55,125	68,900	109,857	133,778
Ticketing service	22,771	29,730	45,036	57,548
Total revenue	343,022	376,834	640,327	692,838
Cost of revenue				
Cost of revenue—Content acquisition costs	176,633	195,875	347,897	383,295
Cost of revenue—Other	25,106	27,440	46,301	52,972
Cost of revenue—Ticketing service	15,259	20,510	29,905	39,128
Total cost of revenue	216,998	243,825	424,103	475,395
Gross profit	126,024	133,009	216,224	217,443
Operating expenses				
Product development	33,560	41,233	69,171	80,821
Sales and marketing	123,589	145,891	241,022	270,993
General and administrative	40,760	57,954	87,284	102,479
Goodwill impairment	—	131,997	—	131,997
Contract termination fees	—	23,467	—	23,467
Total operating expenses	197,909	400,542	397,477	609,757
Loss from operations	(71,885)	(267,533)	(181,253)	(392,314)
Interest expense	(6,247)	(7,404)	(12,422)	(14,785)
Other income, net	255	78	1,117	307
Total other expense, net	(5,992)	(7,326)	(11,305)	(14,478)
Loss before benefit from (provision for) income taxes	(77,877)	(274,859)	(192,558)	(406,792)
Benefit from (provision for) income taxes	1,544	(277)	1,123	(611)
Net loss	(76,333)	(275,136)	(191,435)	(407,403)
Net loss available to common stockholders	$(76,333)	$(289,664)	$(191,435)	$(421,931)
Net loss per common share, basic and diluted	$(0.33)	$(1.20)	$(0.84)	$(1.76)
Weighted-average basic and diluted common shares	229,745	241,320	228,202	239,428

The accompanying notes are an integral part of the condensed consolidated financial statements.

Table of Contents

Pandora Media, Inc.
Condensed Consolidated Statements of Comprehensive Loss
(in thousands)
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2016	**2017**	**2016**	**2017**
Net loss	$(76,333)	$(275,136)	$(191,435)	$(407,403)
Change in foreign currency translation adjustment	(55)	(62)	(288)	129
Change in net unrealized loss on marketable securities	88	7	393	42
Other comprehensive income (loss)	33	(55)	105	171
Total comprehensive loss	$(76,300)	$(275,191)	$(191,330)	$(407,232)

The accompanying notes are an integral part of the condensed consolidated financial statements.

Table of Contents

Pandora Media, Inc.
Condensed Consolidated Statements of Cash Flows
(in thousands) (unaudited)

	Six months ended June 30,	
	2016	**2017**
Operating activities		
Net loss	$(191,435)	$(407,403)
Adjustments to reconcile net loss to net cash used in operating activities		
Goodwill impairment	—	131,997
Depreciation and amortization	27,637	35,115
Stock-based compensation	71,087	68,226
Amortization of premium on investments, net	247	73
Other operating activities	179	186
Amortization of debt discount	8,938	9,799
Bad debt	1,295	9,274
Changes in operating assets and liabilities		
Accounts receivable	12,139	12,594
Prepaid content acquisition costs	(7,271)	6,441
Prepaid expenses and other assets	(8,869)	(11,664)
Accounts payable, accrued and other current liabilities	(17,409)	15,072
Accrued content acquisition costs	26,177	(5,475)
Accrued compensation	5,497	(13,191)
Other long-term liabilities	1	176
Deferred revenue	8,812	4,116
Reimbursement of cost of leasehold improvements	4,397	5,236
Net cash used in operating activities	(58,578)	(139,428)
Investing activities		
Purchases of property and equipment	(34,564)	(8,541)
Internal-use software costs	(14,310)	(10,894)
Changes in restricted cash	(250)	(642)
Purchases of investments	(11,091)	—
Proceeds from maturities of investments	20,007	25,274
Proceeds from sale of investments	500	—
Payments related to acquisitions, net of cash acquired	(676)	—
Net cash (used in) provided by investing activities	(40,384)	5,197
Financing activities		
Proceeds from issuance of redeemable convertible preferred stock	—	172,500
Payments of issuance costs	(32)	(12,625)
Proceeds from employee stock purchase plan	3,837	6,146
Proceeds from exercise of stock options	1,873	3,138
Tax payments from net share settlements of restricted stock units	(2,761)	—
Net cash provided by financing activities	2,917	169,159
Effect of exchange rate changes on cash and cash equivalents	(255)	292
Net (decrease) increase in cash and cash equivalents	(96,300)	35,220
Cash and cash equivalents at beginning of period	334,667	199,944
Less: Cash held for sale	—	(25,583)
Cash and cash equivalents at end of period	$238,367	$209,581
Supplemental disclosures of cash flow information		

Cash paid during the period for interest	$3,228	$4,827
Purchases of property and equipment recorded in accounts payable and accrued liabilities	$5,308	$1,885
Accretion of preferred stock issuance costs	$—	$13,935
Stock dividend payable to preferred stockholders	$—	$595

The accompanying notes are an integral part of the condensed consolidated financial statements.

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements
(unaudited)

1. Description of Business and Basis of Presentation

Pandora—Internet Radio and On-Demand Music Services

Pandora is the world's most powerful music discovery platform, offering a personalized experience for each of our listeners wherever and whenever they want to listen to music—whether through earbuds, car speakers or live on stage. Pandora is available as an ad-supported service, a radio subscription service called Pandora Plus and an on-demand subscription service called Pandora Premium. The majority of our listener hours occur on mobile devices, with the majority of our revenue generated from advertising on our ad-supported service on these devices. We offer both local and national advertisers the opportunity to deliver targeted messages to our listeners using a combination of audio, display and video advertisements. We also generate revenue from subscriptions to Pandora Plus and Pandora Premium. We were incorporated as a California corporation in January 2000 and reincorporated as a Delaware corporation in December 2010. Our principal operations are located in the United States, and we also are located in Australia, New Zealand, Canada and the United Kingdom.

Ticketing Service

We operate our ticketing service through our subsidiary Ticketfly, a leading live events technology company that provides ticketing and marketing software and services for our clients, which are venues and event promoters across North America. Ticketfly's ticketing, digital marketing and analytics software helps promoters book talent, sell tickets and drive in-venue revenue, while Ticketfly's consumer tools help fans find and purchase tickets to events. Ticketfly's revenue primarily consists of service and merchant processing fees from ticketing operations.

In June 2017, we entered into an agreement to sell Ticketfly. Refer to Note 6 "Assets Held for Sale" in the Notes to Condensed Consolidated Financial Statements for further details on the Ticketfly disposition.

As used herein, "Pandora," "we," "our," "the Company" and similar terms include Pandora Media, Inc. and its subsidiaries, unless the context indicates otherwise.

Basis of Presentation

The interim unaudited condensed consolidated financial statements and accompanying notes have been prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP") along with the instructions to Form 10-Q and Article 10 of Securities and Exchange Commission ("SEC") Regulation S-X, and include the accounts of Pandora and our wholly owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation. In the opinion of our management, the interim unaudited condensed consolidated financial statements include all adjustments, which include only normal recurring adjustments, necessary for the fair presentation of our financial position for the periods presented. These interim unaudited condensed consolidated financial statements are not necessarily indicative of the results expected for the full fiscal year or for any subsequent period and should be read in conjunction with the audited consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2016.

Certain changes in presentation have been made to conform the prior period presentation to current period reporting. We have reclassified prepaid content acquisition costs from the prepaid expenses and other assets line item to the prepaid content acquisition costs line item of our condensed consolidated statements of cash flows. We have also

reclassified amortization of internal use-software costs from the product development and sales and marketing line items to the cost of revenue—other and general and administrative line items of our condensed consolidated statements of operations. Lastly, we have also reclassified bad debt and goodwill impairment from the other operating activities line item to the bad debt and goodwill impairment line items of the condensed consolidated statements of cash flows.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and the related disclosures at the date of the financial statements, as well as the reported amounts of revenue and expenses during the periods presented. Estimates are used in several areas including, but not limited to determining accrued content acquisition costs, amortization of minimum guarantees under content acquisition agreements, selling prices for elements sold in multiple-element arrangements,

the allowance for doubtful accounts, the fair value of stock options, market stock units ("MSUs"), stock-settled performance-based restricted stock units ("PSUs"), the Employee Stock Purchase Plan ("ESPP"), the benefit from (provision for) income taxes, the fair value of convertible debt, the fair value of acquired property and equipment, intangible assets and goodwill and the useful lives of acquired intangible assets. To the extent there are material differences between these estimates, judgments or assumptions and actual results, our financial statements could be affected. In many cases, the accounting treatment of a particular transaction is specifically dictated by U.S. GAAP and does not require management's judgment in its application. There are also areas in which management's judgment in selecting among available alternatives would not produce a materially different result.

2. Summary of Significant Accounting Policies

Other than discussed below, there have been no material changes to our significant accounting policies as compared to those described in our Annual Report on Form 10-K for the year ended December 31, 2016.

Stock-Based Compensation—Restricted Stock Units and Stock Options

Stock-based awards granted to employees, including grants of restricted stock units ("RSUs") and stock options, are recognized as expense in our statements of operations based on their grant date fair value. We recognize stock-based compensation expense on a straight-line basis over the service period of the award, which is generally three to four years. We estimate the fair value of RSUs at our stock price on the grant date. We generally estimate the grant date fair value of stock options using the Black-Scholes option-pricing model. The Black-Scholes option-pricing model is affected by our stock price on the date of grant, the expected stock price volatility over the expected term of the award, which is based on projected employee stock option exercise behaviors, the risk-free interest rate for the expected term of the award and expected dividends.

Stock-based compensation expense is recorded in the statement of operations for only those stock-based awards that will vest. In the first quarter of 2017 we adopted new accounting guidance from the Financial Accounting Standards Board ("FASB") on stock compensation, or ASU 2016-09, as described in "Recently Adopted Accounting Standards" below and have elected to account for forfeitures as they occur, rather than estimating expected forfeitures.

Prior to the adoption of ASU 2016-09, we elected to use the "with and without" approach as described in Accounting Standards Codification 740—Income Taxes in determining the order in which tax attributes are utilized. As a result, we previously only recognized a tax benefit from stock-based awards in additional paid-in capital if an incremental tax benefit is realized after all other tax attributes currently available to us have been utilized. In addition, we elected to account for the indirect effects of stock-based awards on other tax attributes, such as the research tax credit, through the statement of operations.

Net Loss per Common Share

Basic net loss per common share is computed by dividing the net loss available to common stockholders by the weighted-average number of shares of common stock outstanding during the period. Diluted net loss per common share is computed by giving effect to all potential shares of common stock, including stock options, restricted stock units, market stock units, performance-based RSUs and instruments convertible into common stock, to the extent dilutive. Basic and diluted net loss per common share were the same for each period presented as the inclusion of all potential common shares outstanding would have been anti-dilutive.

Assets and Liabilities Held for Sale

We consider assets to be held for sale when management approves and commits to a formal plan to actively market the asset for sale at a reasonable price in relation to its fair value, the asset is available for immediate sale in its present condition, an active program to locate a buyer and other actions required to complete the sale have been initiated, the sale of the asset is expected to be completed within one year and it is unlikely that significant changes will be made to the plan. Upon designation as held for sale, we record the carrying value of the assets at the lower of its carrying value or its estimated fair value, less costs to sell. We cease to record depreciation and amortization expense at the time of designation as held for sale. The carrying value of assets and liabilities held for sale were $227.8 million and $43.1 million as of June 30, 2017. We had no assets or liabilities held for sale as of December 31, 2016.

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

Concentration of Credit Risk

For the three and six months ended June 30, 2016 and 2017, we had no customers that accounted for more than 10% of our total revenue. As of December 31, 2016 and June 30, 2017, we had no customers that accounted for more than 10% of our total accounts receivable.

Recently Issued Accounting Standards

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"), which amends the existing accounting standards for revenue recognition. ASU 2014-09 outlines a single comprehensive model for entities to use in accounting for revenue. Under the guidance, revenue is recognized when a company transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The standard is effective for public entities with annual and interim reporting periods beginning after December 15, 2017. Entities have the option of using either a full retrospective or a modified retrospective approach to adopt the guidance. We expect to adopt ASU 2014-09 as of January 1, 2018 and have updated our planned adoption method to the modified retrospective method. We have completed our initial assessment and do not believe there will be a material impact to our condensed consolidated financial statements for the majority of our advertising and subscription revenue arrangements. We are currently continuing to evaluate the impact that the new principal versus agent guidance may have on certain of our advertising revenue arrangements and on our ticketing service revenue arrangements and we are continuing to evaluate the expected impact on our business processes, systems and controls. We expect to complete our assessment of the effects of adopting ASU 2014-09 during 2017, and we will continue our evaluation of ASU 2014-09, including how it may impact new arrangements we enter into as well as new or emerging interpretations of the standard, through the date of adoption.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, Leases (Topic 842) ("ASU 2016-02"). ASU 2016-02 requires lessees to put most leases on their balance sheets but recognize expenses on their income statement and eliminates the real estate-specific provisions for all entities. The guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. We have completed our initial assessment and expect to adopt ASU 2016-02 as of January 1, 2019 using the modified retrospective method. We expect the potential impact of adopting ASU 2016-02 to be material to our lease liabilities and assets on our consolidated balance sheets.

In May 2017, the FASB issued Accounting Standards Update No. 2017-09, Compensation—Stock Compensation (Topic 718), Scope of Modification Accounting ("ASU" 2017-09"). ASU 2017-09 clarifies when changes to the terms or conditions of a share-based payment award must be accounted for as modifications. The guidance is effective prospectively for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years, and early adoption is permitted. We do not expect the adoption of ASU 2017-09 will have a material impact on our financial statements.

Recently Adopted Accounting Standards

In March 2016, the FASB issued Accounting Standards Update No. 2016-09, Compensation—Stock Compensation (Topic 718) ("ASU 2016-09"). ASU 2016-09 requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. Additionally, it allows an employer to repurchase more of an

employee's shares for tax withholding purposes without triggering liability accounting and to make a policy election to account for forfeitures as they occur. We adopted this guidance in the first quarter of 2017 using the modified retrospective transition method. Upon adoption, we recognized the previously unrecognized excess tax benefits as of January 1, 2017 through retained earnings. The previously unrecognized excess tax benefits were recorded as a deferred tax asset, which was fully offset by a valuation allowance. As a result, the net impact resulted in no effect on net deferred tax assets or our accumulated deficit as of January 1, 2017. Without the valuation allowance, the Company’s net deferred tax assets would have increased by approximately $142.0 million. Additionally, we elected to account for forfeitures as they occur, rather than estimating expected forfeitures. The net cumulative effect of this change was an increase to additional paid in capital as of January 1, 2017 by $1.2 million.

In January 2017, the FASB issued Accounting Standards Update No. 2017-04, Intangibles—Goodwill and Other (Topic 350), Simplifying the Test for Goodwill Impairment ("ASU 2017-04"). ASU 2017-04 eliminated the requirement to calculate the implied fair value of goodwill, which is step two of the previous goodwill impairment test, to measure a goodwill impairment charge. By eliminating step two of the goodwill impairment test, entities will record an impairment charge based on the excess of a reporting unit's carrying amount over its fair value. The guidance is effective for calendar-year public business

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

entities that meet the definition of an SEC filer for fiscal years beginning after December 15, 2019, although early adoption is permitted for annual and interim goodwill impairment testing dates following January 1, 2017. We have elected to early adopt this guidance beginning in the second quarter of 2017 using the prospective method, as we believe the elimination of step two of the goodwill impairment test will make testing for goodwill impairment less costly.

3. Cash, Cash Equivalents and Investments

Cash, cash equivalents and investments consisted of the following:

	As of December 31, 2016	As of June 30, 2017
	(in thousands)	
Cash and cash equivalents		
Cash	$144,192	$148,057
Money market funds	55,752	61,524
Total cash and cash equivalents	$199,944	$209,581
Short-term investments		
Corporate debt securities	$37,109	$18,056
Total short-term investments	$37,109	$18,056
Long-term investments		
Corporate debt securities	$6,252	$—
Total long-term investments	$6,252	$—
Cash, cash equivalents and investments	$243,305	$227,637

Our short-term investments have maturities of twelve months or less and are classified as available-for-sale. Our long-term investments have maturities of greater than twelve months and are classified as available-for-sale.

The following tables summarize our available-for-sale securities' adjusted cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category as of December 31, 2016 and June 30, 2017.

	As of December 31, 2016			
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
	(in thousands)			
Money market funds	$55,752	$ —	$ —	$55,752
Corporate debt securities	43,413	3	(55)	43,361
Total cash equivalents and marketable securities	$99,165	$ 3	$ (55)	$99,113

	As of June 30, 2017			
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
	(in thousands)			
Money market funds	$61,524	$ —	$ —	$61,524

Corporate debt securities	18,066		(10)	18,056
Total cash equivalents and marketable securities	$79,590	$ —	$ (10)	$79,580

The following table presents available-for-sale investments by contractual maturity date as of December 31, 2016 and June 30, 2017.

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

	As of December 31, 2016	
	Adjusted Cost	Fair Value
	(in thousands)	
Due in one year or less	$92,914	$ 92,861
Due after one year through three years	6,251	6,252
Total	$99,165	$ 99,113

	As of June 30, 2017	
	Adjusted Cost	Fair Value
	(in thousands)	
Due in one year or less	$79,590	$ 79,580
Total	$79,590	$ 79,580

The following tables summarize our available-for-sale securities' fair value and gross unrealized losses aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position as of December 31, 2016 and June 30, 2017.

	As of December 31, 2016					
	Twelve Months or Less		More than Twelve Months		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	(in thousands)					
Corporate debt securities	$34,257	$ (52)	$4,099	$ (3)	$38,356	$ (55)
Total	$34,257	$ (52)	$4,099	$ (3)	$38,356	$ (55)

	As of June 30, 2017					
	Twelve Months or Less		More than Twelve Months		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	(in thousands)					
Corporate debt securities	$18,056	$ (10)	$ —	$ —	$18,056	$ (10)
Total	$18,056	$ (10)	$ —	$ —	$18,056	$ (10)

Our investment policy requires investments to be investment grade, primarily rated "A1" by Standard & Poor's or "P1" by Moody's or better for short-term investments and rated "A" by Standard & Poor's or "A2" by Moody's or better for long-term investments, with the objective of minimizing the potential risk of principal loss. In addition, the investment policy limits the amount of credit exposure to any one issuer.

The unrealized losses on our available-for-sale securities as of June 30, 2017 were primarily a result of unfavorable changes in interest rates subsequent to the initial purchase of these securities. As of June 30, 2017, we owned 12

securities that were in an unrealized loss position. Based on our cash flow needs, we may be required to sell a portion of these securities prior to maturity. However, we expect to recover the full carrying value of these securities. As a result, no portion of the unrealized losses at June 30, 2017 is deemed to be other-than-temporary and the unrealized losses are not deemed to be credit losses. When evaluating the investments for other-than-temporary impairment, we review factors such as the length of time and extent to which fair value has been below cost basis, the financial condition of the issuer and any changes thereto, and our intent to sell, or whether it is more likely than not we will be required to sell, the investment before recovery of the investment's amortized cost basis. During the three and six months ended June 30, 2017, we did not recognize any impairment charges.

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

4. Fair Value

We record cash equivalents and short-term investments at fair value. Fair value is an exit price, representing the amount that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. Fair value measurements are required to be disclosed by level within the following fair value hierarchy:

Level 1 — Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date.

Level 2 — Inputs (other than quoted prices included in Level 1) are either directly or indirectly observable for the asset or liability through correlation with market data at the measurement date and for the duration of the instrument's anticipated life.

Level 3 — Inputs lack observable market data to corroborate management's estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model.

When determining fair value, whenever possible we use observable market data and rely on unobservable inputs only when observable market data is not available.

The following fair value hierarchy tables categorize information regarding our financial assets and liabilities measured at fair value on a recurring basis at December 31, 2016 and June 30, 2017:

	As of December 31, 2016		
	Fair Value Measurement Using		
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	**Significant Other Observable Inputs (Level 2)**	**Total**
	(in thousands)		
Assets			
Corporate debt securities	$ —	$ 43,361	$ 43,361
Total assets measured at fair value	$ —	$ 43,361	$ 43,361

	As of June 30, 2017		
	Fair Value Measurement Using		
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	**Significant Other Observable Inputs (Level 2)**	**Total**

	(in thousands)		
Assets			
Corporate debt securities	$ —	$ 18,056	$ 18,056
Total assets measured at fair value	$ —	$ 18,056	$ 18,056

Our other cash equivalents and short-term investments are classified as Level 2 within the fair value hierarchy because they are valued using professional pricing sources for identical or comparable instruments, rather than direct observations of quoted prices in active markets. As of December 31, 2016 and June 30, 2017, we held no Level 3 assets or liabilities.

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

Our money market funds are no longer classified within the fair value hierarchy, as the fair values are measured at net asset value using the practical expedient. As of December 31, 2016 and June 30, 2017, the fair values of our money market funds were $55.8 million and $61.5 million.

Refer to Note 8, "Debt Instruments," for the carrying amount and estimated fair value of our convertible senior notes, which are not recorded at fair value as of June 30, 2017.

5. Commitments and Contingencies

Minimum Guarantees and Other Provisions—Content Acquisition Costs

Certain of our content acquisition agreements contain minimum guarantees, and require that we make upfront minimum guarantee payments. During the three and six months ended June 30, 2017, we prepaid $68.8 million and $145.8 million in content acquisition costs related to minimum guarantees, which were offset by amortization of prepaid content acquisition costs of $28.9 million and $105.9 million. As of June 30, 2017, we have future minimum guarantee commitments of $617.2 million, of which $209.7 million will be paid in 2017 and the remainder will be paid thereafter. On a quarterly basis, we record the greater of the cumulative actual content acquisition costs incurred or the cumulative minimum guarantee based on forecasted usage for the minimum guarantee period. The minimum guarantee period is the period of time that the minimum guarantee relates to, as specified in each agreement, which may be annual or a longer period. The cumulative minimum guarantee, based on forecasted usage considers factors such as listening hours, revenue, subscribers and other terms of each agreement that impact our expected attainment or recoupment of the minimum guarantees based on the relative attribution method.

Several of our content acquisition agreements also include provisions related to the royalty payments and structures of those agreements relative to other content licensing arrangements, which, if triggered, could cause our payments under those agreements to escalate. In addition, record labels, publishers and PROs with whom we have entered into direct license agreements have the right to audit our content acquisition payments, and any such audit could result in disputes over whether we have paid the proper content acquisition costs. However, as of June 30, 2017, we do not believe it is probable that these provisions of our agreements discussed above will, individually or in the aggregate, have a material adverse effect on our business, financial position, results of operations or cash flows.

Legal Proceedings

We have been in the past, and continue to be, a party to various legal proceedings, which have consumed, and may continue to consume, financial and managerial resources. We record a liability when we believe that it is both probable that a loss has been incurred and the amount can be reasonably estimated. Our management periodically evaluates developments that could affect the amount, if any, of liability that we have previously accrued and make adjustments as appropriate. Determining both the likelihood and the estimated amount of a loss requires significant judgment, and management’s judgment may be incorrect. We do not believe the ultimate resolution of any pending legal matters is likely to have a material adverse effect on our business, financial position, results of operations or cash flows.

Pre-1972 copyright litigation

On October 2, 2014, Flo & Eddie Inc. filed a class action suit against Pandora Media Inc. in the federal district court for the Central District of California. The complaint alleges misappropriation and conversion in connection with the public performance of sound recordings recorded prior to February 15, 1972. On December 19, 2014, Pandora filed a motion to strike the complaint pursuant to California's Anti-Strategic Lawsuit Against Public Participation ("Anti-SLAPP") statute, which was appealed to the Ninth Circuit Court of Appeals. The district court litigation is currently stayed pending the Ninth Circuit's decision. On December 8, 2016, the Ninth Circuit heard oral argument on the Anti-SLAPP motion. On March 15, 2017, the Ninth Circuit requested certification to the California Supreme Court on the substantive legal questions. The California Supreme Court has accepted certification and opening briefs are due on August 4, 2017.

Between September 14, 2015 and October 19, 2015, Arthur and Barbara Sheridan filed separate class action suits against the Company in the federal district courts for the Northern District of California, District of New Jersey and Northern District of Illinois. The complaints allege a variety of violations of common law and state copyright statutes, common law misappropriation, unfair competition, conversion, unjust enrichment and violation of rights of publicity arising from allegations that we owe royalties for the public performance of sound recordings recorded prior to February 15, 1972. The action in Illinois

was dismissed by the court in June 2017. The actions in California and New Jersey are currently stayed pending the Ninth Circuit's decision in *Flo & Eddie, Inc. v. Pandora Media, Inc*.

On September 7, 2016, Ponderosa Twins Plus One et al. filed a class action suit against the Company alleging claims similar to that of *Flo & Eddie, Inc. v. Pandora Media Inc*. The action is currently stayed in the Northern District of California pending the Ninth Circuit's decision in *Flo & Eddie, Inc. v. Pandora Media, Inc*.

The outcome of any litigation is inherently uncertain. Except as noted above, we do not believe it is probable that the final outcome of the matters discussed above will, individually or in the aggregate, have a material adverse effect on our business, financial position, results of operations or cash flows; however, in light of the uncertainties involved in such matters, there can be no assurance that the outcome of each case or the costs of litigation, regardless of outcome, will not have a material adverse effect on our business.

Indemnification Agreements, Guarantees and Contingencies

In the ordinary course of business, we are party to certain contractual agreements under which we may provide indemnifications of varying scope, terms and duration to customers, vendors, lessors, business partners and other parties with respect to certain matters, including, but not limited to, losses arising out of breach of such agreements, services to be provided by us or from intellectual property infringement claims made by third parties. In addition, we have entered into indemnification agreements with directors and certain officers and employees that will require us, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors, officers or employees. Such indemnification provisions are accounted for in accordance with guarantor's accounting and disclosure requirements for guarantees, including indirect guarantees of indebtedness of others. To date, we have not incurred, do not anticipate incurring and therefore have not accrued for, any costs related to such indemnification provisions.

While the outcome of these matters cannot be predicted with certainty, we do not believe that the outcome of any claims under indemnification arrangements will have a material adverse effect on our business, financial position, results of operations or cash flows.

6. Assets and Liabilities Held for Sale

Ticketfly

In June 2017, we entered into an agreement to sell Ticketfly, our ticketing service segment, to Eventbrite, Inc. ("Eventbrite") for an estimated purchase price of $184.5 million, which includes an aggregate purchase price of $200.0 million, less estimated purchase price adjustments of $10.9 million for certain indemnification provisions and costs to sell of $4.6 million. The $200.0 million aggregate purchase price consists of $150.0 million in cash and $50.0 million in the form of a convertible subordinated promissory note (the "Note"), which are payable and issuable at the closing of the transaction. We expect the sale to be completed in the three months ending September 30, 2017. The purchase price is subject to customary adjustments for working capital and certain indemnification provisions. The Note will be due five years from its issuance date (the "Maturity Date") and will accrue interest at a rate of 6.5% per annum, payable quarterly in cash or stock for the first year, and in cash thereafter. Prior to the Maturity Date, the Note is convertible at the Company's option into shares of Eventbrite's common stock.

As a result of the agreement, we met the requirements to classify the assets and liabilities of Ticketfly as held for sale in the three months ended June 30, 2017. During the three and six months ended June 30, 2017, we recognized

goodwill impairment of $131.7 million for the Ticketfly assets held for sale, which was based on the fair value of these net assets as implied by the estimated purchase price of $184.5 million. We consider the fair value of the net assets to be classified as Level 2 within the fair value hierarchy because Ticketfly is not a publicly traded company. Instead, the fair value was based on other observable inputs, such as the selling price, which represents an exit price. The revenues and expenses of Ticketfly are included in our condensed consolidated statements of operations for the three and six months ended June 30, 2016 and 2017. The following table provides Ticketfly's loss before provision for income taxes for the three and six months ended June 30, 2016 and 2017:

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2016	2017	2016	2017
	(in thousands)			
Loss before benefit from (provision for) income taxes	$8,230	$141,041	$15,851	$151,245

KXMZ

In June 2017, we entered into a purchase agreement to sell KXMZ, an FM radio station based in Rapid City, South Dakota. As a result of the purchase agreement, we met the requirements to classify the assets and liabilities of KXMZ as held for sale in the three months ended June 30, 2017. This did not result in a material impact to our condensed consolidated financial statements.

Assets and Liabilities Held for Sale

The following table provides the carrying amounts of the major classes of assets and liabilities of Ticketfly and KXMZ included in held for sale in our Condensed Consolidated Balance Sheet as of June 30, 2017.

	As of June 30, 2017
Assets held for sale	
Cash and cash equivalents	$25,583
Accounts receivable, net	5,625
Prepaid expenses and other current assets	10,293
Property and equipment, net	5,096
Goodwill	103,474
Intangible assets, net	57,932
Other long-term assets	19,841
Total assets held for sale	$227,844
Liabilities held for sale	
Accounts payable, accrued liabilities and accrued compensation	$5,637
Other current liabilities	28,758
Other long-term liabilities	8,664
Total liabilities held for sale	$43,059

The above assets and liabilities held for sale have been classified as current due to our expectation that the sales will be completed within one year of June 30, 2017. Given that the sales of Ticketfly and KXMZ do not represent a strategic shift in our business, we have not classified the operations of these business as discontinued operations in our Condensed Consolidated Statements of Operations.

7. Goodwill and Intangible Assets

During the three and six months ended June 30, 2017, we entered into agreements to sell Ticketfly and KXMZ and met the requirements to classify the assets and liabilities of Ticketfly and KXMZ as held for sale. As a result of the Ticketfly agreement, we recognized a goodwill impairment of $131.7 million for the Ticketfly assets held for sale,

which was based on the fair value of these net assets as implied by the estimated purchase price of $184.5 million, which includes an aggregate purchase price of $200.0 million, less estimated purchase price adjustments of $10.9 million for certain indemnification provisions and costs to sell of $4.6 million. As a result of the KXMZ agreement, we recognized a goodwill impairment of $0.3 million for the KXMZ assets held for sale, which was based on the fair value of these net assets as implied by the estimated purchase price. We performed goodwill impairment testing on our remaining goodwill, noting no additional impairment.

The changes in the carrying amount of goodwill in each of our reporting segments for the six months ended June 30, 2017, are as follows:

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

	Pandora	Ticketfly	Total
	(in thousands)		
Balance as of December 31, 2016	$71,650	$235,041	$306,691
Goodwill impairment	(300)	(131,697)	(131,997)
Goodwill classified as held for sale	(107)	(103,367)	(103,474)
Effect of currency translation adjustment	—	23	23
Balance as of June 30, 2017	$71,243	$—	$71,243

The following summarizes information regarding the gross carrying amounts and accumulated amortization of intangible assets.

	As of December 31, 2016			As of June 30, 2017			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value	Gross Carrying Amount	Accumulated Amortization	Intangible Assets Held for Sale	Net Carrying Value
	(in thousands)			(in thousands)			
Finite-lived intangible assets							
Patents	$8,030	$ (2,556)	$ 5,474	$8,030	$ (2,923)	$—	$ 5,107
Developed technology	56,162	(13,599)	42,563	56,162	(19,293)	(19,235)	17,634
Customer relationships—clients	37,399	(5,487)	31,912	37,399	(7,449)	(29,950)	—
Customer relationships—users	1,940	(1,288)	652	1,940	(1,732)	(208)	—
Trade names	11,735	(2,104)	9,631	11,735	(2,895)	(8,346)	494
Total finite-lived intangible assets	$115,266	$ (25,034)	$ 90,232	$115,266	$ (34,292)	$(57,739)	$ 23,235
Indefinite-lived intangible assets							
FCC license - Broadcast Radio	$193	$ —	$ 193	$193	$ —	$(193)	$ —
Total intangible assets	$115,459	$ (25,034)	$ 90,425	$115,459	$ (34,292)	$(57,932)	$ 23,235

Note: Amounts may not recalculate due to rounding

Amortization expense of intangible assets was $5.1 million and $4.1 million for the three months ended June 30, 2016 and 2017. Amortization expense of intangible assets was $10.3 million and $9.3 million for the six months ended June 30, 2016 and 2017.

The following is a schedule of future amortization expense related to finite-lived intangible assets as of June 30, 2017.

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

	As of June 30, 2017 (in thousands)
Remainder of 2017	$ 3,827
2018	6,066
2019	5,546
2020	5,251
2021	727
Thereafter	1,818
Total future amortization expense	$ 23,235

8. Debt Instruments

Long-term debt, net consisted of the following:

	As of December 31, 2016	As of June 30, 2017
	(in thousands)	
1.75% convertible senior notes due 2020	$345,000	$345,000
Credit facility	90,000	90,000
Unamortized discount and deferred issuance costs	(92,753)	(82,843)
Long-term debt, net	$342,247	$352,157

Convertible Debt Offering

On December 9, 2015, we completed an unregistered Rule 144A offering for the issuance of $345.0 million aggregate principal amount of our 1.75% Convertible Senior Notes due 2020 (the "Notes"). In connection with the issuance of the Notes, we entered into capped call transactions with the initial purchaser of the Notes and an additional financial institution ("capped call transactions"). The net proceeds from the sale of the Notes were approximately $336.5 million, after deducting the initial purchasers' fees and other estimated expenses. We used approximately $43.2 million of the net proceeds to pay the cost of the capped call transactions.

The Notes are unsecured, senior obligations of Pandora, and interest is payable semi-annually at a rate of 1.75% per annum. The Notes will mature on December 1, 2020, unless earlier repurchased or redeemed by Pandora or converted in accordance with their terms prior to such date. Prior to July 1, 2020, the Notes are convertible at the option of holders only upon the occurrence of specified events or during certain periods as further described in Note 7 "Debt Instruments" in our Annual Report on Form 10-K for the year ended December 31, 2016 thereafter, until the second scheduled trading day prior to maturity, the Notes will be convertible at the option of holders at any time.

The Notes were separated into debt and equity components and assigned a fair value. The value assigned to the debt component is the estimated fair value as of the issuance date of similar debt without the conversion feature. The difference between the cash proceeds and this estimated fair value represents the value which has been assigned to the equity component and recorded as a debt discount. The debt discount is being amortized using the effective interest method over the period from the date of issuance through the December 1, 2020 maturity date. The valuation of the Notes is further described in Note 7 "Debt Instruments" in our Annual Report on Form 10-K for the year ended December 31, 2016.

The following table outlines the effective interest rate, contractually stated interest expense and costs related to the amortization of the discount for the Notes:

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2016	2017	2016	2017
	(in thousands except for effective interest rate)			
Effective interest rate	10.18 %	10.18 %	10.18 %	10.18 %
Contractually stated interest expense	$1,509	$1,493	$3,019	$3,002
Amortization of discount	$4,503	$4,912	$8,938	$9,799

The total estimated fair value of the Notes as of June 30, 2017 was $331.9 million. The fair value was determined using a methodology that combines direct market observations with quantitative pricing models to generate evaluated prices. We consider the fair value of the Notes to be a Level 2 measurement due to the limited trading activity of the Notes.

The closing price of our common stock was $8.92 on June 30, 2017, which was less than the initial conversion price for the Notes of approximately $16.42 per share. As such, the if-converted value of the Notes was less than the principal amount of $345.0 million.

Credit Facility

We are party to a $120.0 million credit facility with a syndicate of financial institutions, which expires on September 12, 2018. In September 2016, we borrowed $90.0 million from the credit facility to enhance our working capital position. The amount borrowed is included in long-term debt on our balance sheet. Interest is payable quarterly at the applicable annual interest rate of 3.81% through September 2017. The applicable interest rate will be adjusted in September 2017.

As of June 30, 2017, we had $1.2 million in letters of credit outstanding and $28.8 million of available borrowing capacity under the credit facility. We are in compliance with all financial covenants associated with the credit facility as of June 30, 2017.

9. Redeemable Convertible Preferred Stock

In June 2017, we entered into an agreement with Sirius XM Radio, Inc. ("Sirius XM") to sell 480,000 shares of Series A redeemable convertible preferred stock ("Series A") for $1,000 per share, with gross proceeds of $480.0 million (the "Sirius XM Investment Agreement"). The Series A shares will be issued in two rounds: an initial closing of 172,500 shares for $172.5 million that occurred on June 9, 2017 upon signing the agreement with Sirius XM, and an additional closing of 307,500 shares for $307.5 million that is subject to antitrust clearance and other customary closing conditions. We expect the additional closing to occur in the fourth quarter of 2017. In the three and six months ended June 30, 2017, total proceeds to the Company from the initial closing, net of preferred stock issuance costs of $13.9 million, were $158.6 million, exclusive of the termination fee paid to KKR Classic Investors L.P. ("KKR"), and certain related expenses, totaling $23.5 million as described below.

Conversion Feature

Holders of the Series A shares have the option, at any time after the additional closing, or if the Sirius XM Investment Agreement is terminated prior to the additional closing, the date of such termination, to convert their shares plus any accrued dividends into common stock. We have the right to settle the conversion in cash, common stock or a combination thereof. The conversion rate for the Series A is initially 95.2381 shares of common stock per each share of Series A, which is equivalent to an initial conversion price of approximately $10.50 per share of our common stock, and is subject to adjustment in certain circumstances. Dividends on the Series A will accrue on a daily basis, whether or not declared, and will be payable on a quarterly basis at a rate of 6% per year. We have the option to pay dividends in cash when authorized by the Board and declared by the Company or accumulate dividends in lieu of paying cash. Dividends accumulated in lieu of paying cash will continue to accrue and cumulate at rate of 6% per year.

Redemption Feature

Under certain circumstances, we will have the right to redeem the Series A on or after the date which is three years after the additional closing or, if the additional closing does not occur, the third anniversary of the initial closing. The Series A holders will have the right to require us to redeem the Series A on or after the date which is five years after the additional closing or, if the additional closing does not occur, the fifth anniversary of the initial closing. Any optional redemption of the Series A will be at a redemption price equal to 100% of the liquidation preference, plus accrued and unpaid dividends to, but excluding, the redemption date. We have the option to redeem the Series A in cash, common stock or a combination thereof.

Fundamental Changes

If certain fundamental changes involving the Company occur, including change in control or liquidation, the Series A will be redeemed subject to certain adjustments, as determined by the date of the fundamental change. The change in control amount is the greater of the redemption value of 100% of the liquidation preference, plus all accrued dividends unpaid through the fifth anniversary of the initial closing, assuming the shares would have remained outstanding through that date, or the price that common stockholders would receive if the Series A shares had been redeemed immediately prior to the announcement of the change in control.

Recognition

Since the redemption of the Series A is contingently or optionally redeemable and therefore not certain to occur, the Series A is not required to be classified as a liability under ASC 480, *Distinguishing Liabilities from Equity*. As the Series A is redeemable at the option of the holders and is redeemable in certain circumstances upon the occurrence of an event that is not solely within the Company's control, we have classified the Series A in the redeemable convertible preferred stock line item in our condensed consolidated balance sheets. We did not identify any embedded features that would require bifurcation from the equity-like host instrument. We have elected to recognize the Series A at the redemption value at each period end, and have recorded the issuance costs through retained earnings as a deemed preferred stock dividend. In addition, we have elected to account for the 6% dividend at the stated rate.

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

	As of June 30, 2017 (in thousands)
Series A redeemable convertible preferred stock	$ 172,500
Issuance costs	(13,935)
Accretion of issuance costs	13,935
Stock dividend payable to preferred stockholders	595
Redeemable convertible preferred stock	$ 173,095

Contract Termination Fees

In May 2017, we entered into an agreement to sell redeemable convertible preferred stock to KKR. In June 2017, in conjunction with the Series A, we terminated the previous contractual commitment to sell redeemable convertible preferred stock to KKR, which resulted in a contract termination fee and related legal and professional fees, totaling $23.5 million. This is included in the contract termination fees line item of our condensed consolidated statements of operations.

10. Stock-based Compensation Plans and Awards

ESPP

The ESPP allows eligible employees to purchase shares of our common stock through payroll deductions of up to 15% of their eligible compensation. The ESPP provides for six-month offering periods, commencing in February and August of each year.

We estimate the fair value of shares to be issued under the ESPP on the first day of the offering period using the Black-Scholes valuation model. The determination of the fair value is affected by our stock price on the first date of the offering period, as well as other assumptions including the risk-free interest rate, the estimated volatility of our stock price over the term of the offering period, the expected term of the offering period and the expected dividend rate. Stock-based compensation expense related to the ESPP is recognized on a straight-line basis over the offering period. Forfeitures are recognized as they occur.

The following assumptions for the Black-Scholes option pricing model were used to determine the per-share fair value of shares to be granted under the ESPP:

	Three months ended June 30,		Six months ended June 30,	
	2016	2017	2016	2017
Expected life (in years)	0.5	0.5	0.5	0.5
Risk-free interest rate	0.41%	0.65%	0.24 - 0.41%	0.44 - 0.65%
Expected volatility	41%	39 %	41 %	39 - 52%
Expected dividend yield	0 %	0 %	0 %	0 %

During the three months ended June 30, 2016 and 2017, we withheld $2.2 million and $3.3 million in contributions from employees and recognized $0.7 million and $1.0 million of stock-based compensation expense related to the ESPP, respectively. During the six months ended June 30, 2016 and 2017, we withheld $3.8 million and $6.1 million in contributions from employees and recognized $1.4 million and $1.9 million of stock-based compensation expense related to the ESPP, respectively. In the six months ended June 30, 2016 and 2017, 611,348 and 547,765 shares of common stock were issued under the ESPP. There were no shares of common stock issued under the ESPP in the three months ended June 30, 2016 and 2017.

Employee Stock-Based Awards

Our 2011 Equity Incentive Plan (the "2011 Plan") provides for the issuance of stock options, restricted stock units and other stock-based awards to our employees. The 2011 Plan is administered by the compensation committee of our board of directors.

Table of Contents
Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

Stock options

We measure stock-based compensation expense for stock options at the grant date fair value of the award and recognize expense on a straight-line basis over the requisite service period, which is generally the vesting period. We estimate the fair value of stock options using the Black-Scholes option-pricing model. During the three months ended June 30, 2016 and 2017, we recorded stock-based compensation expense from stock options of approximately $2.3 million and $4.0 million. During the six months ended June 30, 2016 and 2017, we recorded stock-based compensation expense from stock options of approximately $9.2 million and $5.9 million.

The per-share fair value of each stock option was determined on the grant date using the Black-Scholes option pricing model using the following assumptions:

	Three months ended June 30,		**Six months ended June 30,**	
	2016	**2017**	**2016**	**2017**
Expected life (in years)	N/A	6.00	N/A	5.93 - 6.05
Risk-free interest rate	N/A	1.92%	N/A	1.92 - 2.18%
Expected volatility	N/A	61%	N/A	61%
Expected dividend yield	N/A	0 %	N/A	0 %

There were no options granted in the three and six months ended June 30, 2016.

RSUs

The fair value of RSUs is expensed ratably over the vesting period. RSUs typically have an initial annual cliff vest and then vest quarterly thereafter over the service period, which is generally three to four years. During the three months ended June 30, 2016 and 2017, we recorded stock-based compensation expense from RSUs of approximately $28.1 million and $33.4 million. During the six months ended June 30, 2016 and 2017, we recorded stock-based compensation expense from RSUs of approximately $59.1 million and $58.8 million.

MSUs

In March 2015, the compensation committee of the board of directors granted performance awards consisting of market stock units to certain key executives under our 2011 Plan.

MSUs granted in March 2015 are earned as a function of Pandora’s TSR performance measured against that of the Russell 2000 Index across three performance periods:

- One-third of the target MSUs are eligible to be earned for a performance period that is the first calendar year of the MSU grant (the "One-Year Performance Period");
- One-third of the target MSUs are eligible to be earned for a performance period that is the first two calendar years of the MSU grant (the "Two-Year Performance Period"); and

- Any remaining portion of the total potential MSUs are eligible to be earned for a performance period that is the entire three calendar years of the MSU grant (the "Three-Year Performance Period").

For each performance period, a "performance multiplier" is calculated by comparing Pandora’s TSR for the period to the Russell 2000 Index TSR for the same period, using the average adjusted closing stock price of Pandora stock, and the Russell 2000 Index, for ninety calendar days prior to the beginning of the performance period and the last ninety calendar days of the performance period. In each period, the target number of shares will vest if the Pandora TSR is equal to the Russell 2000 Index TSR. For each percentage point that the Pandora TSR falls below the Russell 2000 Index TSR for the period, the performance multiplier is decreased by three percentage points. The performance multiplier is capped at 100% for the One-Year and Two-Year Performance Periods. However, the full award is eligible for a payout up to 200% of target, less any shares earned in prior periods, in the Three-Year Performance Period. Specifically, for each percentage point that the Pandora TSR exceeds the Russell 2000 Index TSR for the Three-Year Performance Period, the performance multiplier is increased by 2%. As such, the

ability to exceed the target number of shares is determined exclusively with respect to Pandora's three-year TSR during the term of the award.

We have determined the grant-date fair value of the MSUs using a Monte Carlo simulation performed by a third-party valuation firm. We recognize stock-based compensation for the MSUs over the requisite service period, which is approximately three years, using the accelerated attribution method.

There were no MSUs granted in the three or six months ended June 30, 2016 or 2017. During the three months ended June 30, 2016, we recorded approximately $0.2 million in stock-based compensation expense from MSUs. During the three months ended June 30, 2017, we recorded a credit to stock-based compensation expense from MSUs of approximately $0.1 million as a result of executive terminations. During the six months ended June 30, 2016 and 2017, we recorded stock-based compensation expense from MSUs of approximately $0.4 million and $0.2 million.

In February 2016 and January 2017, the compensation committee of the board of directors certified the results of the One-Year Performance Period and Two-Year Performance Period of the 2015 MSU grant, which concluded December 31, 2015 and 2016. During the One-Year Performance Period, our relative TSR declined 26 percentage points relative to the Russell 2000 Index TSR for the period, which resulted in the vesting of the One-Year Performance Period at 22% of the one-third vesting opportunity for the period. During the Two-Year Performance Period, our relative TSR declined 48 percentage points relative to the Russell 2000 Index TSR for the period, which resulted in vesting of the Two-Year Performance Period at 0% of the one-third vesting opportunity for the period.

PSUs

In April and October 2016, the compensation committee of the board of directors granted 2016 Performance Awards consisting of stock-settled performance-based RSUs to certain key executives under our 2011 Plan.

PSUs granted in April and October 2016 have a vesting period that includes a four-year service period, during which one fourth of the awards will vest after one year and the remainder will vest quarterly thereafter. The PSUs are earned when our trailing average ninety-day stock price is equal to or greater than $20.00. If the trailing average ninety-day stock price does not equal or exceed $20.00 on the applicable vesting date, then the portion of the award that was scheduled to vest on such vesting date shall not vest but shall vest on the next vesting date on which the trailing average ninety-day stock price equals or exceeds $20.00. Any portion of the award that remains unvested as of the final vesting date shall be canceled and forfeited.

We have determined the grant-date fair value of the PSUs granted in April and October 2016 using a Monte Carlo simulation performed by a third-party valuation firm. We recognize stock-based compensation for the PSUs over the requisite service period, which is approximately four years, using the accelerated attribution method.

During the three and six months ended June 30, 2016 we granted 1,725,000 PSUs at a total grant-date fair value of $8.7 million. There were no PSUs granted in the three or six months ended June 30, 2017. During the three months ended June 30, 2016 and 2017, we recorded stock-based compensation expense from PSUs of approximately $1.1 million and $0.3 million. During the six months ended June 30, 2016 and 2017, we recorded stock-based compensation expense from PSUs of approximately $1.1 million and $1.4 million.

Stock-based Compensation Expense

Stock-based compensation expense related to all employee and non-employee stock-based awards was as follows:

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2016	**2017**	**2016**	**2017**
	(in thousands)		(in thousands)	
Stock-based compensation expense				
Cost of revenue—Other	$1,544	$814	$3,021	$1,629
Cost of revenue—Ticketing service	67	34	127	63
Product development	7,243	9,422	15,744	17,337
Sales and marketing	15,128	15,102	28,741	28,598
General and administrative	8,450	13,236	23,454	20,599
Total stock-based compensation expense	$32,432	$38,608	$71,087	$68,226

In the six months ended June 30, 2016 and three and six months ended June 30, 2017, we recorded stock-based compensation expense of $6.8 million and $5.4 million related to accelerated awards in connection with executive terminations. The majority of this amount is included in the general and administrative line item of our condensed consolidated statements of operations.

11. Net Loss Per Common Share

Basic net loss per common share is computed by dividing net loss available to common stockholders by the weighted-average number of shares of common stock outstanding during the period.

Diluted net loss per common share is computed by giving effect to all potential shares of common stock, including stock options, restricted stock units, market stock units, performance-based RSUs and instruments convertible into common stock, to the extent dilutive. Basic and diluted net loss per common share were the same for the three and six months ended June 30, 2016 and 2017, as the inclusion of all potential common shares outstanding would have been anti-dilutive.

The following table sets forth the computation of historical basic and diluted net loss per common share:

	Three months ended June 30,		Six months ended June 30,	
	2016	**2017**	**2016**	**2017**
	(in thousands except per share amounts)		(in thousands except per share amounts)	
Numerator				
Net loss	$(76,333)	$(275,136)	$(191,435)	$(407,403)
Less: Stock dividend payable to preferred stockholders	—	(14,528)	—	(14,528)
Net loss available to common stockholders	(76,333)	(289,664)	(191,435)	(421,931)
Denominator				
Weighted-average basic and diluted common shares	229,745	241,320	228,202	239,428
Net loss per common share, basic and diluted	$(0.33)	$(1.20)	$(0.84)	$(1.76)

The following potential common shares outstanding were excluded from the computation of diluted net loss per common share because including them would have been anti-dilutive:

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

	As of June 30,	
	2016	2017
	(in thousands)	
Options to purchase common stock	10,027	9,384
Restricted stock units	23,906	21,739
Performance awards*	2,416	1,993
Shares issuable pursuant to the ESPP	720	589
Total common stock equivalents	37,069	33,705

*Includes potential common shares outstanding for MSUs and PSUs

On June 9, 2017, we entered into an agreement with Sirius XM to sell 480,000 shares of Series A, of which 172,500 shares were issued in the three months ended June 30, 2017. Under the treasury stock method, the Series A will generally have a dilutive impact on earnings per share if our average stock price for the period exceeds approximately $10.50 per share of our common stock, the conversion price of the Series A. For the period from the issuance of the offering through June 30, 2017, the conversion feature of the Series A was anti-dilutive, as our average stock price was less than the conversion price.

On December 9, 2015, we completed an offering of our 1.75% convertible senior notes due 2020. Under the treasury stock method, the Notes will generally have a dilutive impact on earnings per share if our average stock price for the period exceeds approximately $16.42 per share of our common stock, the conversion price of the Notes. For the period from the issuance of the offering of the Notes through June 30, 2017, the conversion feature of the Notes was anti-dilutive, as our average stock price was less than the conversion price.

In connection with the pricing of the Notes, we entered into capped call transactions which increase the effective conversion price of the Notes, and are designed to reduce potential dilution upon conversion of the Notes. Since the beneficial impact of the capped call is anti-dilutive, it is excluded from the calculation of earnings per share. Refer to Note 8 "Debt Instruments" for further details regarding our Notes.

Table of Contents
Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

12. Segment Data and Revenue by Geographic Area

Segment Data

Our two operating segments, which are the same as our two reportable segments, are as follows:

Pandora—Internet radio and on-demand music services

Pandora is the world's most powerful music discovery platform, offering a personalized experience for each of our listeners wherever and whenever they want to listen to music—whether through earbuds, car speakers or home audio/video equipment. Pandora is available as an ad-supported service, a radio subscription service called Pandora Plus and an on-demand subscription service called Pandora Premium. The majority of our listener hours occur on mobile devices, with the majority of our revenue generated from advertising on our ad-supported service on these devices. We offer both local and national advertisers the opportunity to deliver targeted messages to our listeners using a combination of audio, display and video advertisements. We also generate revenue from subscriptions to Pandora Plus and Pandora Premium.

Ticketing service

We operate our ticketing service through our subsidiary Ticketfly, a leading live events technology company that provides ticketing and marketing software and services for clients, which are venues and event promoters, across North America. Ticketfly's ticketing, digital marketing and analytics software helps promoters book talent, sell tickets and drive in-venue revenue, while Ticketfly's consumer tools help fans find and purchase tickets to events. Tickets are primarily sold through the Ticketfly platform but are also sold through other channels such as box offices.

The measurement basis of segment profit or loss is gross profit, as operating expenses and working capital are all managed on an aggregate basis. Total segment assets have not been presented as segment assets are not reported to, used by management to allocate resources to or used to assess performance of the segments.

In June 2017, we entered into an agreement to sell Ticketfly. Refer to Note 6 "Assets Held for Sale" in the Notes to Condensed Consolidated Financial Statements for further details on the Ticketfly disposition.

The following table provides the financial performance of our reportable segments, including a reconciliation of gross profit from segment operations to gross profit from total operations:

	Three months ended June 30,					
	2016			**2017**		
	Pandora	**Ticketfly**	**Total**	**Pandora**	**Ticketfly**	**Total**
	(in thousands)			**(in thousands)**		
Revenues	$320,251	$22,771	$343,022	$347,104	$29,730	$376,834
Cost of revenues	201,739	15,259	216,998	223,315	20,510	243,825
Gross profit	$118,512	$7,512	$126,024	$123,789	$9,220	$133,009
Operating and other expenses			(202,357)			(408,145)
Net loss			$(76,333)			$(275,136)

	Six months ended June 30,					
	2016			2017		
	Pandora	Ticketfly	Total	Pandora	Ticketfly	Total
	(in thousands)			(in thousands)		
Revenues	$595,291	$45,036	$640,327	$635,290	$57,548	$692,838
Cost of revenues	394,198	29,905	424,103	436,267	39,128	475,395
Gross profit	$201,093	$15,131	$216,224	$199,023	$18,420	$217,443
Operating and other expenses			(407,659)			(624,846)
Net loss			$(191,435)			$(407,403)

Table of Contents

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

The following table provides depreciation and amortization costs included in costs of revenues by segment included in the consolidated statements of operations. We did not record depreciation and amortization expense of long-term assets related to the Ticketfly segment in June 2017, subsequent to the date that the related assets qualified as held for sale.

	Three months ended June 30,					
	2016			2017		
	Pandora	Ticketfly	Total	Pandora	Ticketfly	Total
	(in thousands)			(in thousands)		
Depreciation and amortization	$2,432	$ 1,435	$3,867	$5,763	$ 951	$6,714

	Six months ended June 30,					
	2016			2017		
	Pandora	Ticketfly	Total	Pandora	Ticketfly	Total
	(in thousands)			(in thousands)		
Depreciation and amortization	$4,578	$ 2,868	$7,446	$9,110	$ 2,381	$11,491

Revenue by Geographic Area

The following table sets forth revenue by geographic area:

	Three months ended June 30,		Six months ended June 30,	
	2016	2017	2016	2017
	(in thousands)		(in thousands)	
Revenue by geographic area				
United States	$337,363	$372,807	$630,623	$684,102
International	5,659	4,027	9,704	8,736
Total revenue	$343,022	$376,834	$640,327	$692,838

No individual foreign country represented a material portion of our consolidated revenue during the three and six months ended June 30, 2016 and 2017.

13. Restructuring Charges

Reduction in Force

On January 12, 2017, we announced a reduction in force plan affecting approximately 7% of our U.S. employee base, excluding Ticketfly. In the six months ended June 30, 2017, we incurred approximately $6.0 million of cash expenditures, substantially all of which are related to employee severance and benefits costs. In the six months ended June 30, 2017, total reduction in force expenses were $5.6 million, which was lower than cash reduction in force costs due to a credit related to non-cash stock-based compensation expense reversals for unvested equity awards. The reduction in force plan was completed and all amounts were paid in the six months ended June 30, 2017.

Australia and New Zealand Exit Costs

On June 27, 2017, we announced a plan to discontinue business activities in Australia and New Zealand. The related restructuring charges in the three months ended June 30, 2017 relate primarily to a reduction of headcount of approximately 50 employees, which resulted in employee severance and benefits costs, less a credit related to non-cash stock-based compensation expense reversals for unvested equity awards. The dissolution of the Australia and New Zealand business operations is expected to be completed in the three months ended September 30, 2017. We expect to incur additional costs related to the termination of certain advertising agreements and lease agreements and other restructuring charges in the three months ending September 30, 2017. We do not expect these restructuring charges to have a material impact on our financial statements.

Table of Contents

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A")

You should read the following discussion of our financial condition and results of operations in conjunction with the condensed consolidated financial statements and the notes thereto included elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended December 31, 2016 filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act").

This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve substantial risks and uncertainties. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are 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 Exchange Act, including, but not limited to, statements regarding our expectations, beliefs, intentions, strategies, future operations, future financial position, future revenue, projected expenses, plans and objectives of management and economic, competitive and technological trends. In some cases, you can identify forward-looking statements by terms such as "anticipate," "believe," "estimate," "expect," "intend," "may," "might," "plan," "project," "will," "would," "should," "could," "can," "predict," "potential," "continue," "objective," or the negative of these terms, and similar expressions intended to identify forward-looking statements. However, not all forward-looking statements contain these identifying words. These forward-looking statements reflect our current views about future events and involve known risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievement to be materially different from those expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" included in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended December 31, 2016. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements. We qualify all of our forward-looking statements by these cautionary statements. These and other factors could cause our results to differ materially from those expressed in this Quarterly Report on Form 10-Q.

As used herein, "Pandora," the "Company," "we," "our," and similar terms refer to Pandora Media, Inc., unless the context indicates otherwise.

"Pandora" and other trademarks of ours appearing in this report are our property. This report may contain additional trade names and trademarks of other companies. We do not intend our use or display of other companies' trade names or trademarks to imply an endorsement or sponsorship of us by such companies, or any relationship with any of these companies.

Overview

Pandora—Internet Radio and On-Demand Music Services

Pandora is the world's most powerful music discovery platform, offering a personalized experience for each of our listeners wherever and whenever they want to listen to music—whether through earbuds, car speakers or home audio/video equipment. Our vision is to be the definitive source of music discovery and enjoyment for billions of users. Pandora is available as an ad-supported service, a radio subscription service called Pandora Plus and an on-demand subscription service called Pandora Premium. The majority of our listener hours occur on mobile devices, with the majority of our revenue generated from advertising on our ad-supported service on these devices. We offer both local and national advertisers the opportunity to deliver targeted messages to our listeners using a combination of audio, display and video advertisements. We also generate revenue from subscriptions to Pandora Plus and Pandora Premium. Founded by musicians, Pandora also empowers artists with valuable data and tools to help grow their careers and connect with their fans.

At the heart of our service is our set of proprietary personalization technologies, including the Music Genome Project and our playlist generating algorithms. The Music Genome Project is a database of over 1,500,000 uniquely analyzed songs from over 200,000 artists, spanning over 650 genres and sub-genres, which our team of trained musicologists has developed one song at a time by evaluating and cataloging each song's particular attributes. The Music Genome Project database is a subset of our full catalog available to be played. When a listener enters a single song, artist, comedian or genre to start a station, the Pandora service instantly generates a station that plays music or comedy we think that listener will enjoy. Over time, our service has evolved by using data science to further tailor the listener experience based on listener reactions to the recordings we pick. Listeners also have the ability to add variety to and rename stations, which further allows for the personalization of our service. We have integrated this technology into Pandora Premium, giving listeners the ability to search and play any track or album as well as offering unique playlist features tailored to each listener's distinct preferences.

Table of Contents

For the three months ended June 30, 2017, we streamed 5.22 billion hours of radio, and as of June 30, 2017, we had 76.0 million active users during the prior 30-day period and 4.86 million paid subscribers. Since we launched the Pandora service in 2005 our listeners have created over 11 billion stations.

We currently provide the Pandora service through three models:

- *Ad-Supported Service.* Our ad-supported Pandora service allows listeners to access our music and comedy catalogs and personalized playlist generating system for free across all of our delivery platforms. Listeners can obtain more features, such as skips and the ability to replay tracks, by watching an advertisement.

- *Subscription Service—Pandora Plus.* Pandora Plus is a paid, ad-free subscription version of the Pandora service that includes replays, additional skipping, offline listening, higher quality audio on supported devices and longer timeout-free listening.

- *Subscription Service—Pandora Premium.* Our on-demand subscription service, Pandora Premium, launched to select listeners on March 15, 2017, with general availability in the United States on April 18, 2017. Pandora Premium is a paid, ad-free version of the Pandora service that offers a unique, on-demand experience, providing users with the ability to search, play and collect songs and albums, build playlists on their own or with the tap of a button and automatically generates playlists based on the user’s listening activity. The features of Pandora Plus are also included in Pandora Premium.

A key element of our strategy is to make the Pandora service available everywhere that there is internet connectivity. To this end, we make the Pandora service available through a variety of distribution channels. In addition to streaming our service to computers, we have developed Pandora mobile device applications ("apps") for smartphones and mobile operating systems, such as the iPhone and Android and for tablets including the iPad and Android tablets. We distribute those mobile apps free to listeners via app stores.

The development and launch of Pandora Plus and Pandora Premium have and will continue to require significant engineering effort, as well as other resources. In addition, to support the launch of these services we have entered into direct license agreements with major and independent record labels, some of which include substantial minimum guarantee payments. In order for Pandora Plus and Pandora Premium to be successful, we will need to attract subscribers to these new service offerings. The market for subscription-based music services, including on-demand services, is intensely competitive, and our ability to realize a return on our investments in these new service offerings will depend on our ability to leverage the existing audience of our ad-supported service, our brand awareness and our ability to deliver differentiated subscription services with features and functionality that listeners find attractive. Refer to our discussion of these matters in Item 1A—"Risk Factors".

Ticketing Service

We operate our ticketing service through our subsidiary Ticketfly, a leading live events technology company that provides ticketing and marketing software and services for our clients, which are venues and event promoters, across North America. Ticketfly's ticketing, digital marketing and analytics software helps promoters book talent, sell tickets and drive in-venue revenue, while Ticketfly's consumer tools help fans find and purchase tickets to events. Tickets are primarily sold through the Ticketfly platform but are also sold through other channels such as box offices. In the three months ended June 30, 2017, Ticketfly had approximately 48 thousand live events on sale, for which approximately 4.7 million tickets, excluding box office sales, were sold to approximately 2.0 million unique ticket buyers, which resulted in more than $195.0 million in gross transaction value, excluding box office sales.

Ticketfly's platform provides ticketing and marketing services for venues and event promoters across North America and makes it easy for fans to find and purchase tickets to events, and also gives artists a means to more effectively promote their events. We also connect our listeners to events through promotion on our internet radio service.

In June 2017, we entered into an agreement to sell Ticketfly. Refer to Note 6 "Assets Held for Sale" in the Notes to Condensed Consolidated Financial Statements for further details on the Ticketfly disposition.

Recent Events

Pandora Premium

Table of Contents

Our on-demand subscription service, Pandora Premium, launched to select listeners on March 15, 2017, with general availability in the United States on April 18, 2017. Pandora Premium is a paid version of the Pandora service that offers a unique, on-demand experience, providing users with the ability to search, play and collect songs and albums, build playlists on their own or with the tap of a button and automatically generates playlists based on the user's listening activity.

Convertible Redeemable Preferred Stock

In June 2017, we entered into an agreement with Sirius XM Radio, Inc. ("Sirius XM") to sell 480,000 shares of Series A redeemable convertible preferred stock ("Series A") for $1,000 per share, with gross proceeds of $480.0 million (the "Sirius XM Investment"). The Series A shares will be issued in two rounds: an initial closing of 172,500 shares for $172.5 million that occurred on June 9, 2017 upon signing the agreement with Sirius XM, and an additional closing of 307,500 shares for $307.5 million that is subject to antitrust clearance and other customary closing conditions. We expect the additional closing to occur in the fourth quarter of 2017. In the three and six months ended June 30, 2017, total proceeds to the Company from the initial closing, net of preferred stock issuance costs of $13.9 million, were $158.6 million, exclusive of the termination fee paid to KKR Classic Investors L.P. ("KKR"), and certain related expenses, totaling $23.5 million. Refer to Note 9 "Redeemable Convertible Preferred Stock" in the Notes to Condensed Consolidated Financial Statements for further details on the redeemable convertible preferred stock sale.

Ticketfly Disposition

In June 2017, we entered into an agreement to sell Ticketfly, our ticketing service segment, to Eventbrite, Inc. ("Eventbrite") for an estimated purchase price of $184.5 million, which includes an aggregate purchase price of $200.0 million, less estimated purchase price adjustments of $10.9 million for certain indemnification provisions and costs to sell of $4.6 million. The $200.0 million aggregate purchase price consists of $150.0 million in cash and $50.0 million in the form of a convertible subordinated promissory note (the "Note"), which are payable and issuable at the closing of the transaction. We expect the sale to be completed in the three months ended September 30, 2017. The purchase price is subject to customary adjustments for working capital and certain indemnification provisions. The Note will be due five years from its issuance date (the "Maturity Date") and will accrue interest at a rate of 6.5% per annum, payable quarterly in cash or stock for the first year, and in cash thereafter. Prior to the Maturity Date, the Note is convertible at the Company's option into shares of Eventbrite's common stock.

As a result of the purchase agreement, we met the requirements to classify the assets and liabilities of Ticketfly as held for sale in the three months ended June 30, 2017. During the three and six months ended June 30, 2017, we recognized goodwill impairment of $131.7 million for the Ticketfly assets held for sale, which was based on the excess carrying value of goodwill over the fair value of these net assets as implied by the estimated purchase price of $184.5 million. Refer to Note 6 "Assets Held for Sale" in the Notes to Condensed Consolidated Financial Statements for further details on the Ticketfly disposition.

KXMZ Disposition

In June 2017, we entered into an agreement to sell KXMZ, an FM radio station based in Rapid City, South Dakota. As a result of the purchase agreement, we met the requirements to classify the assets and liabilities of KXMZ as held for sale in the three months ended June 30, 2017. This did not result in a material impact to our condensed consolidated financial statements. Refer to Note 6 "Assets Held for Sale" in the Notes to Condensed Consolidated Financial Statements for further details on the KXMZ disposition.

Australia and New Zealand

On June 27, 2017, we announced a plan to discontinue business activities in Australia and New Zealand. The related restructuring charges in the three months ended June 30, 2017 relate primarily to a reduction of headcount of approximately 50 employees, which resulted in employee severance and benefits costs, less a credit related to non-cash stock-based compensation expense reversals for unvested equity awards. The dissolution of the Australia and New Zealand business operations is expected to be completed in the three months ended September 30, 2017. We expect to incur additional costs related to the termination of certain advertising agreements and lease agreements and other restructuring charges in the three months ending September 30, 2017. We do not expect these restructuring charges to have a material impact on our financial statements.

Factors Affecting our Business Model

Content Acquisition Costs

Table of Contents

We pay content acquisition costs based on the terms of direct license agreements with major and independent music labels and distributors for the significant majority of the sound recordings we stream on our ad-supported service, Pandora Plus and Pandora Premium. Depending on the applicable service, these license agreements generally require us to pay either a per-performance fee based on the number of sound recordings we transmit, a percentage of revenue associated with the service, or a per-subscriber minimum amount, all generally subject to certain discounts. Certain of these license agreements require minimum guarantee payments, some of which are paid in advance.

If we have not entered into a direct license agreement with the copyright owner of a particular sound recording that is streamed on our services, we stream that sound recording pursuant to a statutory license and pay the applicable rates set by the Copyright Royalty Board on December 16, 2015 (the "Web IV Proceeding"). The rates for non-subscription services, such as our ad-supported service, were set at $0.0017 per play and the rates for subscription services, such as Pandora Plus, were set at $0.0022 per play for the five-year period from 2016 through 2020. Sound recordings streamed under the statutory license and paid at the Web IV Proceeding rates can only be played in radio mode on our services-these sound recordings cannot be played on-demand or offline and are not eligible for replay or additional skips.

Content acquisition costs for musical works are negotiated with and paid to performing rights organizations ("PROs") such as ASCAP, BMI, SESAC and Global Music Rights and directly to publishing companies. Content acquisition costs for the streaming of musical works on our ad-supported service are calculated such that each copyright holder receives its usage-based and ownership-based share of a royalty pool equal to 20% of the content acquisition costs paid by us for sound recordings on our ad-supported service. Content acquisition costs for the streaming of musical works on our subscription services are equal to the rates determined in accordance with the statutory license set forth in 17 U.S.C. §115 ("Section 115").

The current rate structure for the statutory license for reproduction rights under Section 115 expires at the end of 2017. We are currently one of five commercial music service operators (along with Amazon, Apple, Google and Spotify) participating in rate-setting proceedings in which three judges of the CRB will determine the Section 115 rates for calendar years 2018 to 2022 (the "Phonorecords III Proceedings"). The Nashville Songwriters Association International, the National Association of Music Publishers and George Johnson Music Publishing are also participating in the Phonorecords III Proceedings. A trial before the CRB concluded in April 2017, and the CRB is expected to render a decision prior to the end of 2017. The rates established by the CRB in the Phonorecords III Proceedings may be higher, lower or the same as the rates currently in effect.

The Phonorecords III Proceedings are important to us because our direct licenses with music publishers reference the Section 115 rates. As a result, any increase in the Section 115 rates would increase our content acquisition costs, which, if such increase were substantial, could materially harm our financial condition and hinder our ability to provide interactive features in our services, or cause one or more of our subscription services to not be economically viable.

Ad-Supported Service

Our ad-supported service is monetized through the sale of display, audio and video advertisements to national, regional and local advertisers. We compete with digital advertising networks such as Google and Facebook, other digital media companies and local broadcast radio stations in our advertising business.

Our total number of listener hours is a key driver for both advertising revenue generation opportunities and content acquisition costs, which are the largest component of our ad-related expenses.

- *Advertising Revenue.* Listener hours define the number of opportunities we have to sell advertisements, which we refer to as inventory. Our ability to attract advertisers depends in large part on our ability to offer sufficient inventory within desired demographics.

- *Cost of Revenue—Content Acquisition Costs—Ad-Supported Service.* We pay content acquisition costs to the copyright owners and performers, or their agents, of each sound recording that we stream, as well as to the publishers

and songwriters, or their agents, for the musical works embodied in each of those sound recordings, subject to certain exclusions. The majority of the content acquisition costs related to our ad-supported service are driven by direct license agreements with major and independent labels and distributors, as discussed above in "Factors Affecting Our Business Model—Content Acquisition Costs". Certain of these license agreements include minimum guarantee payments, some of which are paid in advance.

As a result of the structure of our license agreements, our ability to achieve and sustain profitability and operating leverage on our ad-supported service depends on our ability to increase our revenue per thousand listener hours of streaming through increased advertising revenue across all of our delivery platforms.

Subscription Services

Table of Contents

We monetize our subscription services through subscription payments made by users of the services. We drive subscriber growth in our subscription services by providing the world's most powerful music discovery platform, offering a personalized experience for each of our listeners. In addition, we invest in marketing and free-trials to promote our service.

Our total number of paid subscriptions is a key driver for both subscription revenue and content acquisition costs related to our subscription services, which is the largest component of our subscription-related expenses. In order to drive greater subscription revenue, we must increase the number of new subscribers to our subscription services and minimize the number of current subscribers who discontinue their subscriptions.

- *Subscription Revenue*. Our subscription revenue depends upon the number of paid subscriptions we are able to sell and the price that our subscribers pay for those subscriptions. Our ability to attract subscribers depends in large part on our ability to offer features and functionality on our subscription services that are valued by consumers within desired demographics, on terms that are attractive to those consumers, and still enable us to maintain adequate gross margins.

- *Cost of Revenue—Content Acquisition Costs—Subscription Service*. We pay content acquisition costs to the copyright owners, performers, songwriters, or their agents, subject to certain exclusions. The majority of our content acquisition costs related to our subscription service are generally driven by direct license agreements with major and independent labels and distributors, PROs and publishers, as discussed above in "Factors Affecting Our Business Model—Content Acquisition Costs". Certain of these license agreements include minimum guarantee payments, some of which are paid in advance.

Given the structure of our license agreements for our subscription services, the majority of our content acquisition costs increase as subscription revenue increases and are subject to minimum guarantee payments. As such, our ability to achieve and sustain profitability and operating leverage on our subscription services depends on our ability to increase our revenue through increased paid subscriptions on terms that maintain an adequate gross margin. Refer to our discussion of these matters in Item 1A—"Risk Factors" below.

Key Metrics

In the quarter ended December 31, 2016, we began reporting updated key metrics on a prospective basis as a result of a change in our service offerings. We discontinued our previous key metrics as of October 1, 2016. Certain of our new key metrics are not comparable to prior periods given the lack of history of our new service offerings. As such, these metrics have not been presented for, nor compared against, these periods. Refer to the "Key Metrics" section of Item 7—"Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the year ended December 31, 2016 for a summary of the changes in our key metrics.

The below key metrics do not include amounts related to our ticketing service, unless otherwise specifically stated.

Subscription Services—Total

Paid Subscribers

Paid subscribers are defined as the number of distinct users that have current, paid access to our subscription service as of the beginning or the end of the period. Net new subscribers are defined as the net number of distinct new users that have paid for access to our subscription services in the period. We track paid subscribers because it is a key indicator of the growth of our subscription services.

The below table sets forth the detail of the change in paid subscribers in the six months ended June 30, 2017, which includes paid subscribers as of December 31, 2016, net new subscribers during the six months ended June 30, 2017

and paid subscribers as of June 30, 2017.

Table of Contents

	Subscribers (in millions)
Paid subscribers as of December 31, 2016	4.39
Net new paid subscribers	0.47
Paid subscribers as of June 30, 2017	4.86

Penetration rate

Penetration rate is defined as paid subscribers divided by total trailing 30-day active users. We track penetration rate as it is an indicator of the relative scale of our subscriber base. Our penetration rate as of June 30, 2017 was 6.4%.

Average revenue per paid subscriber ("ARPU") and average licensing costs per paid subscriber ("LPU")

ARPU is defined as average monthly revenue per paid subscriber on our subscription services. LPU is defined as average monthly content acquisition costs per paid subscriber on our subscription services. We believe ARPU to be the central top-line indicator for evaluating the results of our monetization efforts on our subscription services. We track LPU because it is a key measure of our ability to manage costs for our subscription services. The below table sets forth our ARPU and LPU for our subscription services for the three and six months ended June 30, 2017.

	Three months ended June 30,		Six months ended June 30,	
	2016	**2017**	**2016**	**2017**
Subscription ARPU	N/A	$4.82	N/A	$4.79
Subscription LPU	N/A	$3.11	N/A	$3.03

Total Service

Listener hours

We track listener hours because it is a key indicator of the growth of our business and the engagement of our listeners. We include listener hours related to our non-radio content offerings in the definition of listener hours. These offerings include non-music content such as podcasts, as well as custom music content such as Pandora Premieres and artist mixtapes. We calculate listener hours based on the total bytes served for each track that is requested and served from our servers, as measured by our internal analytics systems, whether or not a listener listens to the entire track. For non-music content such as podcasts, episodes are divided into approximately track-length parts, which are treated as tracks under this definition. To the extent that third-party measurements of listener hours are not calculated using a similar server-based approach, the third-party measurements may differ from our measurements.

The table below sets forth our total listener hours for the three and six months ended June 30, 2016 and 2017.

	Three months ended June 30,		Six months ended June 30,	
	2016	**2017**	**2016**	**2017**
Service	**(in billions)**		**(in billions)**	
Advertising	4.97	4.19	9.82	8.58
Subscription	0.69	1.03	1.36	1.85

Total	5.66	5.22	11.18	10.43

Active users

We track the number of active users as an additional indicator of the breadth of audience we are reaching at a given time. We define active users as the number of distinct registered users, including subscribers, that have requested audio from our

32

Table of Contents

servers within the trailing 30 days to the end of the final calendar month of the period. The number of active users may overstate the number of unique individuals who actively use our service within a month as one individual may register for, and use, multiple accounts. We include active users who only request non-radio content offerings in the definition of active users.

The table below sets forth our total active users as of June 30, 2016 and 2017.

	As of June 30,	
	2016	2017
	(in millions)	
Active users—all services	78.1	76.0

Advertising-based service

Advertising Revenue per Thousand Listener Hours ("ad RPMs")

We track ad RPMs for our non-subscription, ad-supported service because it is a key indicator of our ability to monetize advertising inventory created by our listener hours. We focus on ad RPMs across all of our delivery platforms. We believe ad RPMs to be the central top-line indicator for evaluating the results of our monetization efforts. Ad RPMs are calculated by dividing advertising revenue by the number of thousands of listener hours of our advertising-based service.

Advertising Content Acquisition Costs per Thousand Listener Hours ("ad LPMs")

We track ad LPMs for our non-subscription, ad-supported service across all delivery platforms. Prior to September 15, 2016, ad LPMs were relatively fixed content acquisition costs with scheduled annual rate adjustments, per thousands of listener hours. Subsequent to September 15, 2016, LPMs are our content acquisition costs as calculated either under the rates set by our license agreements with record labels, PROs and music publishers or under the Web IV rates if we have not entered into a license agreement with the copyright owner of a particular sound recording, in each case per thousands of listener hours.

Period-to-period results should not be regarded as precise nor can they be relied upon as indicative of results for future periods. In addition, as our business matures and in response to technological evolutions, we anticipate that the relevant indicators we monitor for evaluating our business may change.

The table below sets forth our RPMs and LPMs for our ad-supported service for the three and six months ended June 30, 2016 and 2017.

	Three months ended June 30,		Six months ended June 30,	
	2016	2017	2016	2017
Advertising RPMs	$53.34	$66.15	$49.46	$58.34
Advertising LPMs	$30.65	$35.84	$30.56	$34.61

*The calculation of RPMs does not include revenue generated by Ticketfly or Next Big Sound.

Advertising RPMs

For the three and six months ended June 30, 2017 compared to 2016, the increase in ad RPMs was primarily due to a decrease in advertising listener hours as a result of hours control mechanisms and an increase in the number of ads sold per hour.

Advertising LPMs

For the three and six months ended June 30, 2017 compared to 2016, the increase in ad LPMs was primarily due to rate increases related to our direct license agreements with major and independent labels, distributors, PROs and publishers in comparison to the statutory rates used to calculate our content acquisition costs in the three months ended June 30, 2016.

Basis of Presentation and Results of Operations

Table of Contents

The following table presents our results of operations for the periods indicated as a percentage of total revenue. The period-to-period comparisons of results are not necessarily indicative of results for future periods.

	Three months ended June 30,		Six months ended June 30,	
	2016	2017	2016	2017
Revenue				
Advertising	77 %	74 %	76 %	72 %
Subscription and other	16	18	17	19
Ticketing service	7	8	7	8
Total revenue	100	100	100	100
Cost of revenue				
Cost of revenue — Content acquisition costs	51	52	54	55
Cost of revenue — Other (1)	7	7	7	8
Cost of revenue — Ticketing service (1)	4	5	5	6
Total cost of revenue	63	65	66	69
Gross profit	37	35	34	31
Operating expenses				
Product development (1)	10	11	11	12
Sales and marketing (1)	36	39	38	39
General and administrative (1)	12	15	14	15
Goodwill impairment	—	35	—	19
Contract termination fees	—	6	—	3
Total operating expenses	58	106	62	88
Loss from operations	(21)	(71)	(28)	(57)
Interest expense	(2)	(2)	(2)	(2)
Other income, net	—	—	—	—
Total other expense, net	(2)	(2)	(2)	(2)
Loss before provision for (benefit from) income taxes	(23)	(73)	(30)	(59)
Provision for (benefit from) income taxes	—	—	—	—
Net loss	(22)	(73)	(30)	(59)
Net loss available to common stockholders	(22)%	(77)%	(30)%	(61)%

(1) Includes stock-based compensation as follows:				
Cost of revenue - Other	0.5 %	0.2 %	0.5 %	0.2 %
Cost of revenue - Ticketing service	—	—	—	—
Product development	2.1	2.5	2.5	2.5
Sales and marketing	4.4	4.0	4.5	4.1
General and administrative	2.5	3.5	3.7	3.0

Note: Amounts may not recalculate due to rounding

Revenue

Table of Contents

	Three months ended June 30,			Six months ended June 30,		
	2016	2017	$ Change	2016	2017	$ Change
	(in thousands)			(in thousands)		
Revenue						
Advertising	$265,126	$278,204	$ 13,078	$485,434	$501,512	$