Five9, Inc.
Form 10-Q
May 01, 2018

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

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018
OR
o 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: 001-36383

Five9, Inc.
(Exact Name of Registrant as Specified in Its Charter)

Delaware	94- 3394123
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

Bishop Ranch 8
4000 Executive Parkway, Suite 400
San Ramon, CA 94583
(Address of Principal Executive Offices) (Zip Code)
(925) 201-2000
(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 on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes: x No: o

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

Large Accelerated Filer	x	Accelerated Filer	o
Non-accelerated filer	o (Do not check if a smaller reporting Company)	Smaller Reporting Company	o
		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. Yes: o No: 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

As of April 23, 2018, there were 57,683,899 shares of the Registrant’s common stock, par value $0.001 per share, outstanding.

FIVE9, INC.
FORM 10-Q
TABLE OF CONTENTS

Table of Contents

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which involve substantial risks and uncertainties. These statements reflect the current views of our senior management with respect to future events and our financial performance. These forward-looking statements include statements with respect to our business, expenses, strategies, losses, growth plans, product and client initiatives, market growth projections, and our industry. Statements that include the words “expect,” “intend,” “plan,” “believe,” “project,” “forecast,” “estimate,” “may,” “should,” “ar similar statements of a future or forward-looking nature identify forward-looking statements for purposes of the federal securities laws or otherwise.

Forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause our actual results to differ materially from those indicated in these statements. These factors include the information set forth under the caption “Risk Factors” and elsewhere in this report, including the following:

- our quarterly and annual results may fluctuate significantly, may not fully reflect the underlying performance of our business and may result in decreases in the price of our common stock;
- if we are unable to attract new clients or sell additional services and functionality to our existing clients, our revenue and revenue growth will be harmed;
- our recent rapid growth may not be indicative of our future growth, and even if we continue to grow rapidly, we may fail to manage our growth effectively;
- failure to adequately expand our sales force could impede our growth;
- if we fail to manage our technical operations infrastructure, our existing clients may experience service outages, our new clients may experience delays in the deployment of our solution and we could be subject to, among other things, claims for credits or damages;
- security breaches and improper access to or disclosure of our data or our clients’ data, or other cyber attacks on our systems, could result in litigation and regulatory risk, harm our reputation and adversely affect our business;
- the markets in which we participate are highly competitive, and if we do not compete effectively, our operating results could be harmed;
- if our existing clients terminate their subscriptions or reduce their subscriptions and related usage, our revenues and gross margins will be harmed and we will be required to spend more money to grow our client base;
- our growth depends in part on the success of our strategic relationships with third parties and our failure to successfully grow and manage these relationships could harm our business;
- we are establishing a network of master agents and resellers to sell our solution; our failure to effectively develop, manage, and maintain this network could materially harm our revenues;
- we sell our solution to larger organizations that require longer sales and implementation cycles and often demand more configuration and integration services or customized features and functions that we may not offer, any of which could delay or prevent these sales and harm our growth rates, business and operating results;
- because a significant percentage of our revenue is derived from existing clients, downturns or upturns in new sales will not be immediately reflected in our operating results and may be difficult to discern;
- we rely on third-party telecommunications and internet service providers to provide our clients and their customers with telecommunication services and connectivity to our cloud contact center software, any increase in the cost thereof, reduction in efficacy or any failure by these service providers to provide reliable services could cause us to lose customers, increase our customers’ cost of using our solution and subject us to, among other things, claims for credits or damages;
- we have a history of losses and we may be unable to achieve or sustain profitability;
- we may not be able to secure additional financing on favorable terms, or at all, to meet our future capital needs; and
- failure to comply with laws and regulations could harm our business and our reputation.

2

Table of Contents

The foregoing factors should not be construed as exhaustive and should be read together with the other cautionary statements included in this report. If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, our actual results may differ materially from what we anticipate. You should not place undue reliance on our forward-looking statements. Any forward-looking statements you read in this report reflect our views only as of the date of this report with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. We undertake no obligation to update any forward-looking statements made in this report to reflect events or circumstances after the date of this report or to reflect new information or the occurrence of unanticipated events, except as required by law.

Table of Contents

PART I. FINANCIAL INFORMATION
ITEM 1. Financial Statements
FIVE9, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)

	March 31, 2018 (Unaudited)	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 80,676	$ 68,947
Accounts receivable, net	18,534	19,048
Prepaid expenses and other current assets	7,150	4,840
Deferred contract acquisition costs	7,562	—
Total current assets	113,922	92,835
Property and equipment, net	20,876	19,888
Intangible assets, net	957	1,073
Goodwill	11,798	11,798
Other assets	1,120	2,602
Deferred contract acquisition costs — less current portion	17,238	—
Total assets	$ 165,911	$ 128,196
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 5,482	$ 4,292
Accrued and other current liabilities	14,132	11,787
Accrued federal fees	1,331	1,151
Sales tax liability	1,097	1,326
Notes payable	180	336
Capital leases	6,810	6,651
Deferred revenue	13,700	13,975
Total current liabilities	42,732	39,518
Revolving line of credit	32,594	32,594
Sales tax liability — less current portion	979	1,044
Capital leases — less current portion	7,654	7,161
Other long-term liabilities	1,500	1,041
Total liabilities	85,459	81,358
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Preferred stock, $0.001 par value; 5,000 shares authorized, no shares issued and outstanding at March 31, 2018 and December 31, 2017	—	—
Common stock, $0.001 par value; 450,000 shares authorized, 57,654 shares and 56,632 shares issued and outstanding at March 31, 2018 and December 31, 2017, respectively	58	57
Additional paid-in capital	232,277	222,202
Accumulated deficit	(151,883)	(175,421)
Total stockholders' equity	80,452	46,838
Total liabilities and stockholders' equity	$ 165,911	$ 128,196

See accompanying notes to condensed consolidated financial statements.

Table of Contents

FIVE9, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE LOSS
(Unaudited, in thousands, except per share data)

	Three Months Ended	
	March 31, 2018	March 31, 2017
Revenue	$58,905	$47,014
Cost of revenue	24,702	19,971
Gross profit	34,203	27,043
Operating expenses:		
Research and development	7,772	6,847
Sales and marketing	17,478	15,778
General and administrative	9,103	8,860
Total operating expenses	34,353	31,485
Loss from operations	(150)	(4,442)
Other income (expense), net:		
Interest expense	(810)	(882)
Interest income and other	398	118
Total other income (expense), net	(412)	(764)
Loss before income taxes	(562)	(5,206)
Provision for income taxes	45	49
Net loss	$(607)	$(5,255)
Net loss per share:		
Basic and diluted	$(0.01)	$(0.10)
Shares used in computing net loss per share:		
Basic and diluted	56,399	53,688
Comprehensive Income (Loss):		
Net loss and comprehensive loss	$(607)	$(5,255)

See accompanying notes to condensed consolidated financial statements.

Table of Contents

FIVE9, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

	Three Months Ended	
	March 31, 2018	March 31, 2017
Cash flows from operating activities:		
Net loss	$(607)	$(5,255)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	2,320	2,095
Provision for doubtful accounts	48	24
Stock-based compensation	5,325	3,129
Gain on sale of convertible notes held for investment	(312)	—
Non-cash adjustment on investment	(40)	(103)
Amortization of debt discount and issuance costs	20	20
Accretion of interest	16	5
Others	(10)	(8)
Changes in operating assets and liabilities:		
Accounts receivable	519	(1,595)
Prepaid expenses and other current assets	(1,833)	(2,129)
Deferred contract acquisition costs	(1,662)	—
Other assets	(90)	30
Accounts payable	1,181	(95)
Accrued and other current liabilities	2,791	3,119
Accrued federal fees and sales tax liability	(115)	(11)
Deferred revenue	121	909
Other liabilities	325	24
Net cash provided by operating activities	7,997	159
Cash flows from investing activities:		
Purchases of property and equipment	(433)	(514)
Proceeds from sale of convertible notes held for investment	1,923	—
Net cash provided by (used in) investing activities	1,490	(514)
Cash flows from financing activities:		
Proceeds from exercise of common stock options	4,751	793
Payments of notes payable	(157)	(258)
Payments of capital leases	(2,352)	(1,850)
Net cash provided by (used in) financing activities	2,242	(1,315)
Net increase (decrease) in cash and cash equivalents	11,729	(1,670)
Cash and cash equivalents:		
Beginning of period	68,947	58,122
End of period	$80,676	$56,452
Supplemental disclosures of cash flow data:		
Cash paid for interest	$765	$840
Cash paid for income taxes	$33	$21
Non-cash investing and financing activities:		
Equipment obtained under capital lease	$2,635	$2,603
Equipment purchased and unpaid at period-end	$281	$159

See accompanying notes to condensed consolidated financial statements.

Table of Contents

FIVE9, INC.
Notes to Condensed Consolidated Financial Statements (Unaudited)
1. Description of Business and Summary of Significant Accounting Policies
Five9, Inc. and its wholly-owned subsidiaries (the “Company”) is a provider of cloud software for contact centers. The Company was incorporated in Delaware in 2001 and is headquartered in San Ramon, California. The Company has offices in Europe and Asia, which primarily provide research, development, sales, marketing, and client support services.
Basis of Presentation
The accompanying condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (“GAAP”) and applicable rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain information and note disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017. In the opinion of management, the condensed consolidated financial statements reflect all adjustments, which are normal and recurring in nature, necessary for fair financial statement presentation. All intercompany transactions and balances have been eliminated in consolidation.
Certain prior period amounts included in the condensed consolidated financial statements have been reclassified to conform to the current period presentation.
Use of Estimates
The preparation of condensed consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. The significant estimates made by management affect revenue, the allowance for doubtful accounts, loss contingencies, including the Company’s accrual for federal fees and sales tax liability, and accrued liabilities. Management periodically evaluates such estimates and they are adjusted prospectively based upon such periodic evaluation. Actual results could differ from those estimates.
Significant Accounting Policies
The Company’s significant accounting policies are disclosed in its Annual Report on Form 10-K for the year ended December 31, 2017. Other than the accounting policies discussed in Note 2 related to the adoption of ASC 606, there has been no material change to the Company’s significant accounting policies during the three months ended March 31, 2018. See Note 2 for the updated accounting policies.
Recently Adopted Accounting Pronouncements
In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) 2014-09, Revenue from Contracts with Customers: Topic 606, amending revenue recognition guidance and requiring more detailed disclosures to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. ASU 2014-09 also includes Subtopic 340-40, Other Assets and Deferred Costs - Contracts with Customers, which requires the deferral of incremental costs of obtaining a contract with a customer. The Company adopted ASU 2014-09 and its related amendments (collectively “ASC 606”) effective on January 1, 2018 using the modified retrospective method. See Note 2 for disclosure on the impact of adopting this standard.
Recent Accounting Pronouncements Not Yet Effective
In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). Under the new guidance, a lessee will be required to recognize assets and liabilities for both finance, or capital, and operating leases with lease terms of more than 12 months. The ASU also will require disclosures to help investors and other financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. Lessor accounting will

7

Table of Contents

remain largely unchanged from current GAAP. In transition, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach that includes a number of optional practical expedients that entities may elect to apply. This guidance is effective for the Company beginning in the first quarter of 2019. Early adoption is permitted. The Company is currently gathering information and evaluating the impact this guidance will have on its consolidated financial statements.

There are several other new accounting pronouncements issued by the FASB, which the Company will adopt. However, the Company does not believe any of those accounting pronouncements will have a material impact on its consolidated financial position, operating results or statements of cash flows.

2. ASC 606 Adoption Impact and Revenue from Contracts with Customers

ASC 606 Adoption Impact

On January 1, 2018, the Company adopted ASC 606 using the modified retrospective method, applying to all contracts. The Company recognized the cumulative effect of applying the new revenue standard as an adjustment to the opening balance of accumulated deficit at the beginning of 2018. The comparative information has not been restated and continues to be reported under the accounting standards in effect for the period presented, or “ASC 605.” In connection with the adoption of ASC 606, the Company also adopted ASC 340-40, Other Assets and Deferred Costs - Contracts with Customers, which requires the deferral of incremental costs of obtaining a contract with a customer. Collectively, the Company refers to ASC 606 and ASC 340-40 as the "new standard.”

Adoption of the new standard resulted in changes to our accounting policies for revenue recognition, commissions and deferred commissions as discussed below. The Company recorded a net reduction to opening accumulated deficit of $24.1 million as of January 1, 2018 due to the cumulative impact of adopting the new standard. The primary impact of adopting the new standard relates to the deferral of $23.1 million in incremental commission costs of obtaining subscription contracts. Under ASC 605, the Company expensed all commission costs as incurred. Under the new standard, the Company defers all incremental commission costs to obtain the contract, and amortizes these costs over a period of benefit determined to be five years. The remaining $1.0 million impact of adopting the standard relates to revenue being recognized earlier than it would have been under ASC 605.

Practical Expedients and Exemptions

The Company applies a practical expedient that permits the Company to apply Subtopic 340-40 to a single portfolio of contracts, as they are similar in their characteristics, and the financial statement effects of applying Subtopic 340-40 to that portfolio would not differ materially from applying it to the individual contracts within that portfolio.

Additionally, the Company applies a practical expedient of including the remaining value of unsatisfied performance obligations that exist within contracts with original terms of greater than one year.

Impact on the condensed consolidated financial statements

Select condensed consolidated balance sheet line items, which reflects the adoption impact of the new standard, are as follows:

	March 31, 2018		
(in thousands)	As Reported	Balances without adoption of ASC 606	Effect of Change Higher (Lower)
Assets:			
Accounts receivable, net	$18,534	$18,431	$ 103
Prepaid expenses and other current assets	7,150	6,849	301
Deferred contract acquisition costs	24,800	—	24,800
Liabilities:			
Deferred revenue - current	13,700	14,811	(1,111)
Shareholders' Equity:			
Accumulated deficit	(151,883)	(178,198)	26,315

8

Table of Contents

Select condensed consolidated statement of operations line items, which reflects the adoption of the new standard, are as follows:

	Three months ended March 31, 2018		
(in thousands, except per share amounts)	As Reported	Balances without adoption of ASC 606	Effect of Change Higher (Lower)
Revenue	$58,905	$58,152	$ 753
Cost of revenue	24,702	24,457	245
Gross profit	34,203	33,695	508
Sales and marketing	17,478	19,140	(1,662)
Loss from operations	(150)	(2,320)	2,170
Net loss	(607)	(2,777)	2,170
Basic and diluted net loss per share	$(0.01)	$(0.05)	$ 0.04

Select condensed consolidated cash flow line items, which reflects the adoption of the new standard, are as follows:

	Three months ended March 31, 2018		
(in thousands)	As Reported	Balances without adoption of ASC 606	Effect of Change Higher (Lower)
Accounts receivable	$519	$ 622	$ (103)
Prepaid expenses and other current assets	(1,833)	(1,532)	(301)
Deferred contract acquisition costs	(1,662)	—	(1,662)
Deferred revenue	121	1,232	(1,111)
Net cash provided by operating activities	7,997	7,997	—

Changes in Accounting Policies

Revenue Recognition

Revenue is recognized when control of the promised services are transferred to customers, in an amount that reflects the consideration that the Company expects to receive in exchange for those services. The Company generates all of its revenue from contracts with customers. In contracts with multiple performance obligations, it identifies each performance obligation and evaluates whether the performance obligations are distinct within the context of the contract at contract inception. Performance obligations that are not distinct at contract inception are combined. The Company allocates the transaction price to each distinct performance obligation proportionately based on the estimated standalone selling price for each performance obligation. The Company then looks to how services are transferred to the customer in order to determine the timing of revenue recognition. Most services provided under the Company’s agreements result in the transfer of control over time.

The Company’s revenue consists of subscription services and related usage as well as professional services. The Company charges clients subscription fees, usually billed on a monthly basis, for access to the Company’s VCC solution. The monthly subscription fees are primarily based on the number of agent seats, as well as the specific VCC functionalities and applications deployed by the client. Agent seats are defined as the maximum number of named agents allowed to concurrently access the VCC cloud platform. Clients typically have more named agents than agent seats. Multiple named agents may use an agent seat, though not simultaneously. Substantially all of the Company’s clients purchase both subscriptions and related telephony usage. A small percentage of the Company's clients subscribe to its platform but purchase telephony usage directly from a wholesale telecommunications service provider. The Company does not sell telephony usage on a stand-alone basis to any client. The related usage fees are based on the volume of minutes used for inbound and outbound client interactions. The Company also offers bundled plans, generally for smaller deployments, whereby the client is charged a single monthly fixed fee per agent seat that includes both subscription and unlimited usage in the contiguous 48 states and, in some cases, Canada. Professional services revenue is derived primarily from VCC implementations, including application configuration, system integration, optimization, education and training services. Clients are not permitted to take possession of the Company’s software.

Table of Contents

The Company offers monthly, annual and multiple-year contracts to its clients, generally with 30 days' notice required for changes in the number of agent seats and sometimes with a minimum number of agent seats required. Larger clients typically choose annual contracts, which generally include an implementation and ramp period of several months. Fixed subscription fees (including bundled plans) are generally billed monthly in advance, while related usage fees are billed in arrears. Support activities include technical assistance for the Company's solution and upgrades and enhancements to the VCC cloud platform on a when-and-if-available basis, which are not billed separately.

The Company generally requires advance deposits from its clients based on estimated usage when such usage is not billed as part of a bundled plan. Any unused portion of the deposit is refundable to the client upon termination of the arrangement, provided all amounts due have been paid. All fees, except usage deposits, are non-refundable

Professional services are primarily billed on a fixed-fee basis and are performed by the Company directly or, alternatively, clients may also choose to perform these services themselves or engage their own third-party service providers.

The estimation of variable consideration for each performance obligation requires us to make some subjective judgments. In the early stages of our larger contracts, the Company must estimate variable consideration to be included in the transaction fee, to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved, in order to allocate the overall transaction fee on a relative stand-alone selling price basis to its multiple performance obligations. This requires the estimate of unit quantities, especially during the initial ramp period of the contract, during which the Company bills under an 'actual usage' model for subscription-related services.

The Company recognizes revenue on fixed fee professional services performance obligations based on the proportion of labor hours expended compared to the total hours expected to complete the related performance obligation. The determination of the total labor hours expected to complete the performance obligations involves some judgment, influencing the initial stand-alone selling price estimate as well as the timing of professional services revenue recognition, although this uncertainty is typically resolved in a short time frame.

When a contract with a customer is signed, the Company assesses whether collection of the fees under the arrangement is probable. The Company assesses collection based on a number of factors, including past transaction history and the creditworthiness of the client. The Company maintains a revenue reserve for potential credits to be issued in accordance with service level agreements or for other revenue adjustments.

The revenue recognition standards include guidance relating to any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer and may include, but is not limited to, sales, use, value added and excise taxes. The Company records Universal Service Fund, or USF, contributions and other regulatory costs on a gross basis in its consolidated statements of operations and comprehensive loss and records surcharges and sales, use and excise taxes billed to its clients on a net basis. The cost of gross USF contributions payable to the Universal Service Administrative Company, or USAC, and suppliers is presented as a cost of revenue in the condensed consolidated statements of operations and comprehensive loss. Surcharges and sales, use and excise taxes incurred in excess of amounts billed to the Company's clients are presented in general and administrative expense in the condensed consolidated statements of operations and comprehensive loss.

Table of Contents

Disaggregation of Revenue

The Company disaggregates its revenue by geographic region. See Note 11 for more information.

Contract Balances

The following table provides information about receivables, contract assets and contract liabilities from contracts with customers (in thousands):

	March 31, 2018
Receivables	$ 18,534
Deferred contract acquisition costs	24,800
Short-term contract assets	785
Short-term contract liabilities (deferred revenue)	13,700

The Company receives payments from customers based upon billing cycles. Invoice payment terms are usually 30 days or less. Accounts receivable are recorded when the right to consideration becomes unconditional.

Deferred contract acquisition costs are recorded when incurred and are amortized over a customer benefit period of five years.

Contract assets include amounts related to the Company’s contractual right to consideration for performance obligations not yet invoiced and is included in prepaid and other current assets in the condensed consolidated balance sheets. The Company had no asset impairment charges related to contract assets in the period.

Contract liabilities are comprised of amounts billed in advance of performance under the contract, and are realized with the associated revenue recognized under the contract.

Significant changes in the contract assets and the contract liabilities balances during the period are as follows (in thousands):

	Three Months Ended March 31, 2018	
	Contract Assets Increase (Decrease)	Contract Liabilities Increase (Decrease)[1]
Revenue recognized that was included in the contract liability (deferred revenue) balance at January 1, 2018	$ —	$ (6,440)
Increase due	—	6,572

to invoicing in current period, excluding amounts recognized as revenue during the period		
Transferred to receivables from contract assets recognized at January 1, 2018	(86)	—
Additional contract assets recognized, net of reclassification to receivables	135	—
Performance obligations satisfied in previous periods (transition adjustment)	736	(407)

(1) Comprised of deferred revenue

Deferred Contract Acquisition Costs

In connection with the adoption of ASC 340-40, the Company is required to capitalize certain contract acquisition costs consisting primarily of commissions paid when contracts are signed and related incremental fringe benefits. As of January 1, 2018, the date of ASC 340-40 adoption, the Company had $23.1 million capitalized in deferred contract acquisition costs related to contracts where the benefit period had not yet expired. In the three months ended March 31, 2018, amortization from amounts capitalized was $1.9 million and amounts expensed as incurred was $0.5 million. The Company had no impairment loss in relation to costs capitalized.

11

Table of Contents

Remaining Performance Obligations

As of March 31, 2018, the aggregate amount of the total transaction price allocated in contracts with original duration of greater than one year to the remaining performance obligations was $56.5 million. The Company expects to recognize revenue on approximately three-quarters of the remaining performance obligation over the next 24 months, with the balance recognized thereafter. The Company has elected the optional exemption which allows for the exclusion of the amounts for remaining performance obligations that are part of contracts with an original expected duration of one year or less. Such remaining performance obligations represent the unsatisfied or partially unsatisfied performance obligations pursuant to ASC 606.

3. Fair Value Measurements

The Company carries cash equivalents consisting of money market funds at fair value on a recurring basis. Fair value is based on the price that would be received from selling an asset in an orderly transaction between market participants at the measurement date. Fair value is estimated by applying the following hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

Level 1 — Observable inputs which include unadjusted quoted prices in active markets for identical assets.

Level 2 — Observable inputs other than Level 1 inputs, such as quoted prices for similar assets, quoted prices for identical or similar assets in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are based on management's assumptions, including fair value measurements determined by using pricing models, discounted cash flow methodologies or similar techniques.

The fair value of assets carried at fair value was determined using the following inputs (in thousands):

	March 31, 2018		
	Total	Level 1	Level 3
Assets			
Cash equivalents			
Money market funds	$20,132	$20,132	$—
Other Assets			
Embedded conversion option held for investment	$—	$—	$—

	December 31, 2017		
	Total	Level 1	Level 3
Assets			
Cash equivalents			
Money market funds	$20,092	$20,092	$—
Other Assets			
Embedded conversion option held for investment	$984	$—	$984

In March 2018, the Company received proceeds of $1.9 million from the conversion and sales of convertible notes with carrying value of $1.6 million. Proceeds from the sale of the investment total $2.1 million. The Company expects to receive the remainder of the proceeds in 2019.

There were no assets or liabilities measured at fair value on a non-recurring basis as of March 31, 2018.

Table of Contents

4. Financial Statement Components

Cash and cash equivalents consisted of the following (in thousands):

	March 31, 2018	December 31, 2017
Cash	$ 60,544	$ 48,855
Money market funds	20,132	20,092
Cash and cash equivalents	$ 80,676	$ 68,947

As of March 31, 2018, the Company was required to maintain $25.0 million of unrestricted cash and cash equivalents deposited with two lenders in connection with its credit agreement as a compensating balance. See Note 6.

Accounts receivable, net consisted of the following (in thousands):

	March 31, 2018	December 31, 2017
Trade accounts receivable	$ 16,678	$ 17,481
Unbilled trade accounts receivable, net of advance client deposits	1,884	1,600
Allowance for doubtful accounts	(28)	(33)
Accounts receivable, net	$ 18,534	$ 19,048

Prepaid expenses and other current assets consisted of the following (in thousands):

	March 31, 2018	December 31, 2017
Prepaid expenses	$ 4,431	$ 2,437
Other current assets	1,934	2,403
Contract assets	785	—
Prepaid expenses and other current assets	$ 7,150	$ 4,840

Property and equipment, net consisted of the following (in thousands):

	March 31, 2018	December 31, 2017
Computer and network equipment	$ 49,780	$ 47,195
Computer software	7,387	6,974
Internal-use software development costs	500	500
Furniture and fixtures	1,433	1,282
Leasehold improvements	817	801
Property and equipment	59,917	56,752
Accumulated depreciation and amortization	(39,041)	(36,864)
Property and equipment, net	$ 20,876	$ 19,888

Depreciation and amortization expense associated with property and equipment was $2.2 million and $2.0 million for the three months ended March 31, 2018 and 2017, respectively.

Property and equipment capitalized under capital lease obligations consist primarily of computer and network equipment and was as follows (in thousands):

	March 31, 2018	December 31, 2017
Gross	$ 49,167	$ 46,624
Less: accumulated depreciation and amortization	(32,149)	(30,438)
Total	$ 17,018	$ 16,186

Table of Contents

Accrued and other current liabilities consisted of the following (in thousands):

	March 31, 2018	December 31, 2017
Accrued compensation and benefits	$ 11,153	$ 8,657
Accrued expenses	2,979	3,130
Accrued and other current liabilities	$ 14,132	$ 11,787

5. Intangible Assets

The components of intangible assets were as follows (in thousands):

	March 31, 2018			December 31, 2017		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Developed technology	$2,460	$ (1,565)	$ 895	$2,460	$ (1,478)	$ 982
Customer relationships	520	(463)	57	520	(437)	83
Domain names	50	(45)	5	50	(42)	8
Total	$3,030	$ (2,073)	$ 957	$3,030	$ (1,957)	$ 1,073

Amortization expense for intangible assets was $0.1 million for each of the three months ended March 31, 2018 and 2017.

As of March 31, 2018, the expected future amortization expense for intangible assets was as follows (in thousands):

Period	Expected Future Amortization Expense
2018	$ 326
2019	351
2020	280
Total	$ 957

6. Debt

2016 Loan and Security Agreement

On August 1, 2016, or the Effective Date, the Company entered into a loan and security agreement, or the 2016 Loan and Security Agreement, with the lenders party thereto and City National Bank, as agent for such lenders. The 2016 Loan and Security Agreement provides for a revolving line of credit, or the Revolving Credit Facility, of up to $50.0 million and matures on August 1, 2019. On the Effective Date, the Company borrowed $32.6 million under the 2016 Loan and Security Agreement. The proceeds were used to extinguish existing indebtedness under all prior Loan and Security Agreements and for working capital and other general corporate purposes.

Loans under the 2016 Loan and Security Agreement bear a variable annual interest rate of the prime rate plus 0.50%, subject to a 0.25% increase if the Company’s adjusted EBITDA is negative at the end of any fiscal quarter. The Company has agreed to pay a fee of 0.25% per annum on the unused portion of the Revolving Credit Facility as well as an anniversary fee of $31,250 on each of the first and second anniversaries of the Effective Date. The Company is accreting the total estimation of unused fees and anniversary fees evenly over the full term of the 2016 Loan and Security Agreement. Under the terms of the 2016 Loan and Security Agreement, the outstanding balance cannot exceed the Company’s trailing four months of MRR (monthly recurring revenue including subscription and usage) multiplied by the average trailing 12 month dollar based retention rate (calculated on the same basis as in the Company’s periodic reports filed with the SEC). As of March 31, 2018, the outstanding principal balance under the

14

Table of Contents

2016 Loan and Security Agreement was $32.6 million, which is included in 'Revolving line of credit' in the condensed consolidated balance sheets. As of March 31, 2018, the amount available for additional borrowings was $17.4 million. The Company incurred approximately $0.2 million in fees that were directly attributable to the issuance of this credit facility. These costs are deferred and included within 'Prepaid expenses and other current assets' and 'Other assets' in the Company's condensed consolidated balance sheets and being amortized to interest expense on a straight-line basis over three years starting from the Effective Date of the Revolving Credit Facility.

The obligations of the Company under the 2016 Loan and Security Agreement are guaranteed by the Company's subsidiary, Five9 Acquisition. The Company's obligations under the 2016 Loan and Security Agreement and Five9 Acquisition's obligations under its guaranty are secured by a first priority perfected security interest in and lien on substantially all of the Company's and Five9 Acquisition's assets. The 2016 Loan and Security Agreement contains certain customary covenants, including the requirement that the Company maintain $25.0 million of unrestricted cash deposited with the lenders for the term of the agreement, a minimum liquidity ratio of unrestricted cash and accounts receivable to the outstanding amounts under the 2016 Loan and Security Agreement, as well as customary events of default. Under the 2016 Loan and Security Agreement, the Company is also prohibited from declaring dividends or making other distributions on capital stock. The Company was in compliance with these covenants as of March 31, 2018.

FCC Civil Penalty

In June 2015, the Company entered into a consent decree with the Federal Communications Commission, or FCC, Enforcement Bureau, in which the Company agreed to pay a civil penalty of $2.0 million to the U.S. Treasury in twelve equal quarterly installments starting in July 2015 without interest. As a result, the Company discounted the $2.0 million liability, which was accrued in the third quarter of 2014 for the then tentative civil penalty, to its present value of $1.7 million at an annual interest rate of 12.75% to reflect the imputed interest and reclassified this discounted liability from 'Accrued federal fees' to 'Notes payable.' The $0.3 million discount was recorded as a reduction to general and administrative expense in the three months ended June 30, 2015 and is being recognized as interest expense over the payment term of the civil penalty. As of March 31, 2018 and December 31, 2017, the outstanding civil penalty payable was $0.2 million and $0.3 million, respectively, of which the net carrying value was $0.2 million and $0.3 million, respectively, and is included as 'Notes payable' in the accompanying condensed consolidated balance sheets.

As of March 31, 2018 and December 31, 2017, the Company's outstanding debt is summarized as follows (in thousands):

	March 31, 2018	December 31, 2017
Note payable - FCC civil penalty, gross	$ 167	$ 333
Less: discount	(1)	(7)
Note payable, net carrying value	166	326
Revolving line of credit	32,594	32,594
Interest accretion under 2016 line of credit	14	10
Total debt, net carrying value	$ 32,774	$ 32,930
Less: current portion of debt *	$ (180)	$ (336)
Total debt, less current portion **	$ 32,594	$ 32,594

* Included in 'Notes payable' in the condensed consolidated balance sheets.

** Included 'Revolving line of credit' in the condensed consolidated balance sheets.

Maturities of the Company's outstanding debt as of March 31, 2018 are as follows (in thousands):

Period

	Amount to Mature
2018	$167
2019	32,594
Total	$32,761

Table of Contents

7. Stockholders' Equity

Capital Structure

The Company is authorized to issue 450,000,000 shares of common stock with a par value of $0.001 per share. As of March 31, 2018 and December 31, 2017, the Company had 57,653,677 and 56,631,647 shares of common stock issued and outstanding, respectively.

The Company is also authorized to designate and issue up to 5,000,000 shares of preferred stock with a par value of $0.001 per share in one or more series without stockholder approval and to fix the rights, preferences, privileges and restrictions thereof. As of March 31, 2018 and December 31, 2017, the Company had no shares of preferred stock issued and outstanding.

Warrants

As of March 31, 2018 and December 31, 2017, the Company had outstanding warrants to purchase 13,013 shares of common stock with a weighted-average exercise price of $5.76 per share. The warrants outstanding as of March 31, 2018 will expire on October 18, 2023.

Common Stock Reserved for Future Issuance

Shares of common stock reserved for future issuance related to outstanding equity awards, common stock warrants, and employee equity incentive plans were as follows (in thousands):

	March 31, 2018
Stock options outstanding	3,491
Restricted stock units outstanding	2,427
Shares available for future grant under 2014 Plan	9,272
Shares available for future issuance under ESPP	1,937
Common stock warrants outstanding	13
Total shares of common stock reserved	17,140

Equity Incentive Plans

Prior to its initial public offering ("IPO"), the Company granted stock options under its Amended and Restated 2004 Equity Incentive Plan, as amended (the "2004 Plan").

In March 2014, the Company's board of directors and stockholders approved the 2014 Equity Incentive Plan ("2014 Plan") and 5,300,000 shares of common stock were reserved for issuance under the 2014 Plan. In addition, on the first day of each year beginning in 2015 and ending in 2024, the 2014 Plan provides for an annual automatic increase to the shares reserved for issuance in an amount equal to 5% of the total number of shares outstanding on December 31st of the preceding calendar year or a lesser number as determined by the Company's board of directors. Pursuant to the automatic annual increase, 2,831,582 additional shares were reserved under the 2014 Plan on January 1, 2018.

No further grants were made under the 2004 Plan once the 2014 Plan became effective on April 3, 2014. Upon the effectiveness of the 2014 Plan, all shares reserved for future issuance under the 2004 Plan became available for issuance under the 2014 Plan. After the IPO, any forfeited or expired shares that would have otherwise returned to the 2004 Plan instead return to the 2014 Plan.

The 2004 Plan and the 2014 Plan are described in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

Table of Contents

Stock Options

A summary of the Company's stock option activity during the three months ended March 31, 2018 is as follows (in thousands, except years and per share data):

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value
Outstanding as of December 31, 2017	4,047	$ 8.00		
Options granted (weighted average grant date fair value of $14.02 per share)	237	30.08		
Options exercised	(786)	6.04		
Options forfeited or expired	(7)	4.71		
Outstanding as of March 31, 2018	3,491	$ 9.95	6.5	$ 69,323

The Company has computed the aggregate intrinsic value amounts disclosed in the above table based on the difference between the exercise price of the options and the closing market price of the Company's common stock of $29.79 per share as of March 31, 2018 for all in-the-money options outstanding.

Restricted Stock Units

A summary of the Company's restricted stock unit ("RSU") activity during the three months ended March 31, 2018 is as follows (in thousands, except per share data):

	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Outstanding as of December 31, 2017	2,033	$ 7.65
RSUs granted	656	29.48
RSUs vested and released	(236)	10.02
RSUs forfeited	(26)	14.32
Outstanding as of March 31, 2018	2,427	$ 17.56

Employee Stock Purchase Plan

The Company's 2014 Employee Stock Purchase Plan ("ESPP") became effective on April 3, 2014 and is described in the Company's Annual Report on Form 10-K for the year ended December 31, 2017. The number of shares of common stock originally reserved for issuance under the ESPP was 880,000 shares, which will increase automatically each year, beginning on January 1, 2015 and continuing through January 1, 2024, by the lesser of (i) 1% of the total number of shares of the Company's common stock outstanding on December 31 of the preceding calendar year; (ii) 1,000,000 shares of common stock (subject to adjustment to reflect any split or combination of the Company's common stock); or (iii) such lesser number as determined by the Company's board of directors. Pursuant to the automatic annual increase, 566,316 additional shares were reserved under the ESPP on January 1, 2018.

During the three months ended March 31, 2018, no shares were purchased under the ESPP.

Table of Contents

Stock-Based Compensation

Stock-based compensation expenses for the three months ended March 31, 2018 and 2017 were as follows (in thousands):

	Three Months Ended	
	March 31, 2018	March 31, 2017
Cost of revenue	$678	$ 434
Research and development	877	637
Sales and marketing	1,362	928
General and administrative	2,408	1,130
Total stock-based compensation	$5,325	$ 3,129

As of March 31, 2018, unrecognized stock-based compensation expenses by award type and their expected weighted-average recognition periods are summarized in the following table (in thousands, except years).

	Stock Option	RSU	ESPP
Unrecognized stock-based compensation expense	$12,467	$41,974	$220
Weighted-average amortization period	2.7 years	3.2 years	0.1 years

The Company recognizes stock-based compensation expense that is calculated based upon awards that have vested, reduced for actual forfeitures. All stock-based compensation for equity awards granted to employees and non-employee directors is measured based on the grant date fair value of the award.

The Company values RSUs at the closing market price of its common stock on the date of grant. The Company estimates the fair value of each stock option and purchase right under the ESPP granted to employees on the date of grant using the Black-Scholes option-pricing model and using the assumptions noted in the below table. The weighted-average assumptions used to value stock options granted during the three months ended March 31, 2018 and 2017 were as follows:

Stock Options	Three Months Ended	
	March 31, 2018	March 31, 2017
Expected term (years)	6.0	6.0
Volatility	45 %	49 %
Risk-free interest rate	2.7%	2.0 %
Dividend yield [(1)]	—	—

(1) The Company has not paid, and does not anticipate paying, cash dividends on its shares of common stock. Accordingly, the expected dividend yield is zero.

8. Net Loss Per Share

Basic net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the period, and excludes any dilutive effects of employee stock-based awards and warrants. As the Company had net losses for the three months ended March 31, 2018 and 2017, all potentially issuable common shares were determined to be anti-dilutive.

Table of Contents

The following table presents the calculation of basic and diluted net loss per share (in thousands, except per share data).

	Three Months Ended	
	March 31, 2018	March 31, 2017
Net loss	$(607)	$(5,255)
Weighted-average shares of common stock outstanding	56,399	53,688
Basic and diluted net loss per share	$(0.01)	$(0.10)

The following securities were excluded from the calculation of diluted net loss per share because their effect would have been anti-dilutive (in thousands).

	March 31, 2018	March 31, 2017
Stock options	3,491	5,127
Restricted stock units	2,427	2,607
Common stock warrants	13	13
Total	5,931	7,747

9. Income Taxes

The provision for income taxes for the three months ended March 31, 2018 and 2017 was approximately $45 thousand and $49 thousand, respectively. The provision for income taxes consisted primarily of foreign income taxes.

For the three months ended March 31, 2018 and 2017, the provision for income taxes differed from the statutory amount primarily due to the Company realizing no benefit for current year losses due to maintaining a full valuation allowance against its domestic net deferred tax assets.

The realization of tax benefits of deferred tax assets is dependent upon future levels of taxable income, of an appropriate character, in the periods the items are expected to be deductible or taxable. Based on the available objective evidence, the Company does not believe it is more likely than not that the net deferred tax assets will be realizable. Accordingly, the Company has provided a full valuation allowance against the domestic net deferred tax assets as of March 31, 2018 and December 31, 2017. The Company intends to maintain the remaining valuation allowance until sufficient positive evidence exists to support a reversal of, or decrease in, the valuation allowance.

During the three months ended March 31, 2018, there were no material changes to the total amount of unrecognized tax benefits.

10. Commitments and Contingencies

Commitments

The Company’s principal commitments consist of future payment obligations under capital leases to finance data centers and other computer and networking equipment purchases, debt agreements (see Note 6), operating lease agreements for office space, research and development, and sales and marketing facilities, and agreements with third parties to provide co-location hosting, telecommunication usage and equipment maintenance services. These commitments as of December 31, 2017 are disclosed in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017, and did not change materially during the three months ended March 31, 2018 except for the acquisition of certain additional data center and network equipment and software under multiple capital leases, and certain hosting and telecommunications agreements. As of March 31, 2018, the total minimum future payment commitments under these capital leases added during the three months ended March 31, 2018 were approximately $3.7 million, of which $1.1 million is due during the remainder of 2018, with the remaining $2.6 million due in 2019 to 2021.

During the three months ended March 31, 2018, the Company entered into various hosting and telecommunications agreements for terms of 12 to 36 months commencing on various dates in 2018. These

19

Table of Contents

agreements require the Company to make monthly payments over the service term in exchange for certain network services. The Company's total minimum future payment commitments under these agreements are $2.1 million.

Universal Services Fund Liability

During the third quarter of 2012, the Company determined that based on its business activities, it is classified as a telecommunications service provider for regulatory purposes and it should make direct contributions to the federal USF and related funds based on revenues it receives from the resale of interstate and international telecommunications services. In order to comply with the obligation to make direct contributions, the Company made a voluntary self-disclosure to the FCC Enforcement Bureau and registered with the USAC, which is charged by the FCC with administering the USF. The Company filed exemption certificates with its wholesale telecommunications service providers in order to eliminate its obligation to reimburse such wholesale telecommunications service providers for their USF contributions calculated on services sold to the Company. In April 2013, the Company began remitting required contributions on a prospective basis directly to USAC.

The Company's registration with USAC subjects it to assessments for unpaid USF contributions, as well as interest thereon and civil penalties, due to its late registration and past failure to recognize its obligation as a USF contributor and as an international carrier. The Company is required to pay assessments for periods prior to the Company's registration. As of December 31, 2012, the total past due USF contribution being imposed by USAC and accrued by the Company for the period from 2003 through 2012 was $8.1 million, of which $4.7 million was undisputed and $3.4 million was disputed. The Company subsequently updated its filings and increased the liability related to 2008 through 2012 by $0.5 million, arriving at a new total of $3.9 million in disputed liability. In July 2013, the Company and USAC agreed to a financing arrangement for $4.1 million of the undisputed $4.7 million of the unpaid USF contributions whereby the Company issued to USAC a promissory note payable in the principal amount of the $4.1 million and paid off the remaining undisputed $0.6 million. The Company had fully paid the promissory note as of January 2017.

In January 2017, the FCC's Wireline Competition Bureau ruled in the Company's favor with respect to most of the disputed amount. In September 2017, USAC issued a credit to the Company reflecting the FCC's ruling for the $3.1 million of the $3.9 million in disputed liability. In addition, USAC reversed the interest and penalties related to the disputed liability of $3.1 million. The remaining $0.8 million in dispute involves USAC's assessment of liability for the period of 2003 through 2007, which was prior to the five year window during which the Company was required to maintain financial records for USF contribution purposes. The Company filed a Request for Review (a form of appeal) of this disputed amount with the FCC's Wireline Competition Bureau in 2013, which remains pending. If the Request for Review is not resolved in the Company's favor, it is possible that the Company will be held to the back assessments of $0.8 million, which includes interest and penalties on that amount.

As of March 31, 2018, the accrued liability on the remaining disputed assessments, including interest and penalties for the period of 2003 through 2007, was $0.8 million offset by $0.7 million in other USF credits.

State and Local Taxes and Surcharges

In April 2012, the Company commenced collecting and remitting sales taxes on sales of subscription services in all the U.S. states in which it determined it was obligated to do so. During the first quarter of 2015, the Company conducted an updated sales tax review of the taxability of sales of its subscription services. As a result, the Company determined that it may be obligated to collect and remit sales taxes on such sales in four additional states. Based on its best estimate of the probable sales tax liability in those four states relating to its sales of subscription services during the period 2011 through 2014, during the three months ended March 31, 2015, the Company recorded a general and administrative expense of $0.6 million to accrue for such taxes.

During 2013, the Company analyzed its activities and determined it may be obligated to collect and remit various state and local taxes and surcharges on its usage-based fees. The Company had not remitted state and local taxes on usage-based fees in any of the periods prior to 2014 and therefore accrued a sales tax liability for this contingency. In January 2014, the Company commenced paying such taxes and surcharges to certain state authorities. In June 2014, the Company commenced collecting state and local taxes or surcharges on usage-based fees from its clients on a current basis and remitting such taxes to the applicable U.S. state taxing authorities.

As of March 31, 2018 and December 31, 2017, the Company had total accrued liabilities of $1.4 million and $1.5 million, respectively, for such contingent sales taxes and surcharges that were not being collected from its clients but may be imposed by various taxing authorities, of which $0.3 million and $0.4 million, respectively, were included in current “Sales tax liability” on the condensed consolidated balance sheets, and the remaining were included in non-current “Sales tax liability” on the condensed consolidated balance sheets. The Company’s estimate of the probable loss incurred under this contingency is based on its analysis of the source location of its usage-based fees and the regulations and rules in each tax jurisdiction.

Legal Matters

The Company is involved in various legal and regulatory matters arising in the normal course of business. In management’s opinion, resolution of these matters is not expected to have a material impact on the Company’s consolidated results of operations, cash flows, or its financial position. However, due to the uncertain nature of legal matters, an unfavorable resolution of a matter could materially affect the Company’s future consolidated results of operations, cash flows or financial position in a particular period. The Company expenses legal fees as incurred.

Indemnification Agreements

In the ordinary course of business, the Company enters into agreements of varying scope and terms pursuant to which it agrees to indemnify clients, 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 the Company or from intellectual property infringement claims made by third parties. In addition, the Company has entered into indemnification agreements with directors and certain officers and employees that will require it, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors, officers or employees. Other than as described below, no demands have been made upon the Company to provide indemnification under such agreements and there are no claims that it is aware of that could have a material effect on the consolidated balance sheet, consolidated statement of operations and comprehensive loss, or consolidated statements of cash flows.

On October 27, 2016, the Company received notice from Lance Fried, a former officer and director of Face It, Corp., of his claim for indemnification by the Company (as successor in interest to Face It), and for advancement of all legal fees and expenses he incurs in connection with the defense of a lawsuit captioned Melcher, et al. v. Five9, Inc., et al., No. 16-cv-02440, in the U.S. District Court for the Southern District of California. In the lawsuit, plaintiff Carl Melcher, a purported former stockholder of Face It, and his related investment entity Melcher Family Limited Partnership, allege that Face It repurchased the plaintiffs’ stock in September 2013 before Five9 acquired Face It, and that in connection with the repurchase, Fried made material misstatements or omissions to Melcher, by failing to disclose that Face It allegedly was in concurrent discussions about a potential sale of the company to Five9. The lawsuit alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, as well as various claims under state law and common law. To date, the Company has advanced Mr. Fried $62 thousand in connection with this claim. However, the Company disputes that Mr. Fried is entitled to advancement in connection with the Melcher litigation. On July 31, 2017, Mr. Fried filed a complaint against the Company in the Court of Chancery for the State of Delaware, in which he alleges that the Company breached advancement obligations to him. On December 7, 2017, the Delaware Chancery Court stayed Mr. Fried’s advancement lawsuit, in favor of arbitration. On January 9, 2018, the Company received Mr. Fried’s demand for arbitration against the Company with respect to the same matter. Regardless of the outcome of Mr. Fried’s advancement action against the Company, Mr. Fried is required to reimburse the Company for any amounts advanced to him if it is ultimately determined that Mr. Fried is not entitled to indemnification in connection with the Melcher litigation. In addition, the Company believes that it has indemnification rights against the former stockholders of Face It (including Mr. Fried) for all losses that are incurred by the Company in connection with the Melcher litigation, including without limitation, amounts incurred to indemnify or advance the legal fees and expenses of Mr. Fried pursuant to his indemnification claim against the Company.

Table of Contents

11. Geographical Information

The following table is a summary of revenues by geographic region based on client billing address and has been estimated based on the amounts billed to clients during the periods presented (in thousands).

	Three Months Ended	
	March 31, 2018	March 31, 2017
United States	$55,171	$ 44,358
International	3,734	2,656
Total revenue	$58,905	$ 47,014

The following table summarizes total property and equipment, net in the respective locations (in thousands).

	March 31, 2018	December 31, 2017
United States	$ 19,091	$ 17,949
International	1,785	1,939
Property and equipment, net	$ 20,876	$ 19,888

Table of Contents

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

You should read the following discussion in conjunction with the condensed consolidated financial statements and 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, 2017.

Overview

We are a pioneer and leading provider of cloud software for contact centers, facilitating more than three billion interactions between our more than 2,000 clients and their customers per year. We believe we achieved this leadership position through our expertise and technology, which has empowered us to help organizations of all sizes transition from legacy on-premise contact center systems to our cloud solution. Our solution, which is comprised of our Virtual Contact Center, or VCC, cloud platform and applications, allows simultaneous management and optimization of customer interactions across voice, chat, email, web, social media and mobile channels, either directly or through our application programming interfaces, or APIs. Our VCC cloud platform routes each customer interaction to an appropriate agent resource, and delivers relevant customer data to the agent in real-time to optimize the customer experience. Unlike legacy on-premise contact center systems, our solution requires minimal up-front investment and can be rapidly deployed and adjusted depending on our client's requirements.

Since founding our business in 2001, we have focused exclusively on delivering cloud contact center software. We initially targeted smaller contact center opportunities with our telesales team and, over time, invested in expanding the breadth and depth of the functionality of our cloud platform to meet the evolving requirements of our clients. In 2009, we made a strategic decision to expand our market opportunity to include larger contact centers. This decision drove further investments in research and development and the establishment of our field sales team to meet the requirements of these larger contact centers. We believe this shift has helped us diversify our client base, while significantly enhancing our opportunity for future revenue growth. To complement these efforts, we have also focused on building client awareness and driving adoption of our solution through marketing activities, which include internet advertising, digital marketing campaigns, social marketing, trade shows, industry events and telemarketing.

We provide our solution through a SaaS business model with recurring subscriptions. We offer a comprehensive suite of applications delivered on our VCC cloud platform that are designed to enable our clients to manage and optimize interactions across inbound and outbound contact centers. We primarily generate revenue by selling subscriptions and related usage of our VCC cloud platform. We charge our clients monthly subscription fees for access to our solution, primarily based on the number of agent seats, as well as the specific functionalities and applications our clients deploy. We define agent seats as the maximum number of named agents allowed to concurrently access our solution. Our clients typically have more named agents than agent seats, and multiple named agents may use an agent seat, though not simultaneously. Substantially all of our clients purchase both subscriptions and related telephony usage from us. A small percentage of our clients subscribe to our platform but purchase telephony usage directly from wholesale telecommunications service providers. We do not sell telephony usage on a stand-alone basis to any client. The related usage fees are based on the volume of minutes for inbound and outbound interactions. We also offer bundled plans, generally for smaller deployments, where the client is charged a single monthly fixed fee per agent seat that includes both subscription and unlimited usage in the contiguous 48 states and, in some cases, Canada. We offer monthly, annual and multiple-year contracts to our clients, generally with 30 days' notice required for changes in the number of agent seats. Our clients can use this notice period to rapidly adjust the number of agent seats used to meet their changing contact center volume needs, including to reduce the number of agent seats to zero. As a general matter, this means that a client can effectively terminate its agreement with us upon 30 days' notice. Our larger clients typically choose annual contracts, which generally include an implementation and ramp period of several months. Fixed subscription fees, including bundled plans, are generally billed monthly in advance, while related usage fees are billed in arrears. For the three months ended March 31, 2018 and 2017, subscription and related usage fees accounted for 92% and 94% of our revenue, respectively. The remainder was comprised of professional services revenue from the implementation and optimization of our solution.

Key GAAP Operating Results

Our revenue increased to $58.9 million for the three months ended March 31, 2018 from $47.0 million for the three months ended March 31, 2017. Revenue growth has primarily been driven by our larger clients. For each of the three months ended March 31, 2018 and 2017, no single client accounted for more than 10% of our total revenue. As of March 31, 2018, we had over 2,000 clients across multiple industries. Our clients' subscriptions generally range in

Table of Contents

size from fewer than 10 agent seats to approximately 2,000 agent seats. We had net loss of $0.6 million in the three months ended March 31, 2018 compared to net loss of $5.3 million in the three months ended March 31, 2017.

We have continued to make significant expenditures and investments, including in sales and marketing, research and development and infrastructure. We primarily evaluate the success of our business based on revenue growth, adjusted EBITDA and the efficiency and effectiveness of our investments. The growth of our business and our future success depend on many factors, including our ability to continue to expand our client base, particularly in larger opportunities, grow revenue from our existing client base, develop innovative products and features, and expand internationally. While these areas represent significant opportunities for us, they also pose risks and challenges that we must successfully address in order to sustain the growth of our business and improve our operating results. In order to pursue these opportunities, we anticipate that we will continue to expand our operations and headcount in the near term.

Due to our continuing investments to grow our business, increase our sales and marketing efforts, pursue new opportunities, enhance our solution and build our technology, we expect our cost of revenue and operating expenses to increase in absolute dollars in future periods. However, we expect these expenses to decrease as a percentage of revenue as we grow our revenue and gain economies of scale by increasing our client base without direct incremental development costs and by utilizing more of the capacity of our data centers.

Key Operating and Non-GAAP Financial Performance Metrics

In addition to measures of financial performance presented in our condensed consolidated financial statements, we monitor the key metrics set forth below to help us evaluate growth trends, establish budgets, measure the effectiveness of our sales and marketing efforts and assess operational efficiencies.

Annual Dollar-Based Retention Rate

We believe that our Annual Dollar-Based Retention Rate provides insight into our ability to retain and grow revenue from our clients, and is a measure of the long-term value of our client relationships. Our Annual Dollar-Based Retention Rate is calculated by dividing our Retained Net Invoicing by our Retention Base Net Invoicing on a monthly basis, which we then average using the rates for the trailing twelve months for the period being presented. We define Retention Base Net Invoicing as recurring net invoicing from all clients in the comparable prior year period, and we define Retained Net Invoicing as recurring net invoicing from that same group of clients in the current period. We define recurring net invoicing as subscription and related usage revenue excluding the impact of service credits, reserves and deferrals. Historically, the difference between recurring net invoicing and our subscription and related usage revenue has been within 10%.

The following table shows our Annual Dollar-Based Retention Rate for the periods presented:

	Twelve Months Ended	
	March 31, 2018	March 31, 2017
Annual Dollar-Based Retention Rate	98%	99%

Our Dollar-Based Retention Rate declined year over year primarily due to the termination of one customer for non-payment and the bankruptcy of another customer.

Adjusted EBITDA

We monitor adjusted EBITDA, a non-GAAP financial measure, to analyze our financial results and believe that it is useful to investors, as a supplement to U.S. GAAP measures, in evaluating our ongoing operational performance and enhancing an overall understanding of our past financial performance. We believe that adjusted EBITDA helps illustrate underlying trends in our business that could otherwise be masked by the effect of the income or expenses that we exclude from adjusted EBITDA. Furthermore, we use this measure to establish budgets and operational goals for managing our business and evaluating our performance. We also believe that adjusted EBITDA provides an additional tool for investors to use in comparing our recurring core business operating results over multiple periods with other companies in our industry.

Adjusted EBITDA should not be considered in isolation from, or as a substitute for, financial information prepared in accordance with U.S. GAAP and our calculation of adjusted EBITDA may differ from that of other

24

Table of Contents

companies in our industry. We compensate for the inherent limitations associated with using adjusted EBITDA through disclosure of these limitations, presentation of our financial statements in accordance with U.S. GAAP and reconciliation of adjusted EBITDA to the most directly comparable U.S. GAAP measure, net loss. We calculate adjusted EBITDA as net loss before (1) depreciation and amortization, (2) stock-based compensation, (3) interest income, expense and other, (4) provision for income taxes, and (5) other unusual items that do not directly affect what we consider to be our core operating performance.

The following table shows a reconciliation from net loss to Adjusted EBITDA for the periods presented (in thousands):

	Three Months Ended	
	March 31, 2018	March 31, 2017
Net loss	$(607)	$(5,255)
Non-GAAP adjustments:		
Depreciation and amortization [1]	2,320	2,095
Stock-based compensation [2]	5,325	3,129
Interest expense	810	882
Interest income and other	(398)	(118)
Legal settlement [3]	—	1,700
Legal and indemnification fees related to settlement [3]	—	135
Provision for income taxes	45	49
Adjusted EBITDA	$7,495	$2,617

(1) Depreciation and amortization expenses included in our results of operations are as follows (in thousands):

	Three Months Ended	
	March 31, 2018	March 31, 2017
Cost of revenue	$1,794	$ 1,576
Research and development	194	206
Sales and marketing	29	30
General and administrative	303	283
Total depreciation and amortization	$2,320	$ 2,095

(2) See Note 7 of the notes to condensed consolidated financial statements for stock-based compensation expense included in our results of operations for the periods presented.

(3) Represents settlement amount, legal and indemnification fees related to the settlement of a litigation.

Key Components of Our Results of Operations

Revenue

Our revenue consists of subscription and related usage as well as professional services. We consider our subscription and related usage to be recurring revenue. This recurring revenue includes fixed subscription fees for the delivery and support of our VCC cloud platform, as well as related usage fees. The related usage fees are based on the volume of minutes for inbound and outbound client interactions. We also offer bundled plans, generally for smaller deployments, where the client is charged a single monthly fixed fee per agent seat that includes both subscription and unlimited usage in the contiguous 48 states and, in some cases, Canada. We offer monthly, annual and multiple-year contracts for our clients, generally with 30 days' notice required for changes in the number of agent seats. Our clients can use this notice period to rapidly adjust the number of agent seats used to meet their changing contact center volume needs, including to reduce the number of agent seats to zero. As a general matter, this means that a client can effectively terminate its agreement with us upon 30 days’ notice.

Fixed subscription fees, including plans with bundled usage, are generally billed monthly in advance, while variable usage fees are billed in arrears. Fixed subscription fees are recognized on a straight-line basis over the

Table of Contents

applicable term, predominantly the monthly contractual billing period. Support activities include technical assistance for our solution and upgrades and enhancements on a when and if available basis, which are not billed separately. Variable subscription related usage fees for non-bundled plans are billed in arrears based on client-specific per minute rate plans and are recognized as actual usage occurs. We generally require advance deposits from clients based on estimated usage. All fees, except usage deposits, are non-refundable.

In addition, we generate professional services revenue from assisting clients in implementing our solution and optimizing use. These services include application configuration, system integration and education and training services. Professional services are primarily billed on a fixed-fee basis and are typically performed by us directly. In limited cases, our clients choose to perform these services themselves or engage their own third-party service providers to perform such services. Professional services are recognized as the services are performed using the proportional performance method, with performance measured based on labor hours, provided all other criteria for revenue recognition are met.

The adoption of ASC 606, the new revenue recognition guidance, in January 2018 did not have a material impact on the recognition or timing of revenue. See Note 2 of notes to condensed consolidated financial statements in this report for additional information.

Cost of Revenue

Our cost of revenue consists primarily of personnel costs (including stock-based compensation), fees that we pay to telecommunications providers for usage, USF contributions and other regulatory costs, depreciation and related expenses of the servers and equipment, costs to build out and maintain co-location data centers, and allocated office and facility costs and amortization of acquired technology. Cost of revenue can fluctuate based on a number of factors, including the fees we pay to telecommunications providers, which vary depending on our clients' usage of our VCC cloud platform, the timing of capital expenditures and related depreciation charges and changes in headcount. We expect to continue investing in our network infrastructure and operations and client support function to maintain high quality and availability of service, resulting in absolute dollar increases in Cost of Revenue. As our business grows, we expect to realize economies of scale in network infrastructure, personnel and client support.

Operating Expenses

We classify our operating expenses as research and development, sales and marketing, and general and administrative expenses.

Research and Development. Our research and development expenses consist primarily of salary and related expenses (including stock-based compensation) for personnel related to the development of improvements and expanded features for our services, as well as quality assurance, testing, product management and allocated overhead. We expense research and development expenses as they are incurred except for internal-use software development costs that qualify for capitalization. We believe that continued investment in our solution is important for our future growth, and we expect research and development expenses to increase in absolute dollars in the foreseeable future, although these expenses as a percentage of our revenue are expected to decrease over time.

Sales and Marketing. Sales and marketing expenses consist primarily of salaries and related expenses (including stock-based compensation) for personnel in sales and marketing, sales commissions, as well as advertising, marketing, corporate communications, travel costs and allocated overhead. Prior to the adoption of ASC 606, we expensed sales commissions associated with the acquisition of client contracts as incurred in the period the contract is acquired. Upon the adoption of ASC 606 in January 2018, a significant amount of our sales commission expenses have been deferred over an expected benefit period of five years as required by ASC 340-40, Other Assets and Deferred Costs - Contracts with Customers. See Note 2 of notes to condensed consolidated financial statements in this report for additional information. We believe it is important to continue investing in sales and marketing to continue to generate revenue growth. Accordingly, while we expect sales and marketing expenses to increase in absolute dollars as we continue to support our growth initiatives, with the adoption of ASC 606 in January 2018, we expect sales and marketing expense as a percentage of revenue to decrease in our consolidated statements of operations due to the deferral of a significant portion of sales commissions as required by ASC 340-40.

General and Administrative. General and administrative expenses consist primarily of salary and related expenses (including stock-based compensation) for management, finance and accounting, legal, information systems and human resources personnel, professional fees, compliance costs, other corporate expenses and allocated overhead.

Table of Contents

We expect that general and administrative expenses will fluctuate in absolute dollars from period to period, but decline as a percentage of revenue over time.

Other Income (Expense), Net

Other income (expense), net consists primarily of interest expense associated with our debt and capital leases. We expect interest expense for our capital leases to increase as a result of our continued capital spending funded by capital leases.

Provision for Income Taxes

Our provision for income taxes consists primarily of corporate income taxes resulting from profits generated in foreign jurisdictions by our wholly-owned subsidiaries, along with state income taxes payable in the United States. We do not expect the new legislation signed into law by President Trump in December 2017 to have a significant impact on our future income tax provision.

Results of Operations for the Three Months Ended March 31, 2018 and 2017

Based on the condensed consolidated statements of operations and comprehensive loss set forth in this Quarterly Report on Form 10-Q, the following table sets forth our operating results as a percentage of revenue for the periods indicated:

	Three Months Ended	
	March 31, 2018	March 31, 2017
Revenue	100 %	100 %
Cost of revenue	42 %	42 %
Gross profit	58 %	58 %
Operating expenses:		
Research and development	13 %	15 %
Sales and marketing	30 %	34 %
General and administrative	15 %	18 %
Total operating expenses	58 %	67 %
Loss from operations	— %	(9)%
Other income (expense), net:		
Interest expense	(1)%	(2)%
Interest income and other	— %	— %
Total other income (expense), net	(1)%	(2)%
Loss before income taxes	(1)%	(11)%
Provision for income taxes	— %	— %
Net loss	(1)%	(11)%

Revenue

	Three Months Ended			
	March 31, 2018	March 31, 2017	$ Change	% Change
	(in thousands, except percentages)			
Revenue	$58,905	$47,014	$11,891	25 %

The increase in revenue for the three months ended March 31, 2018 compared to the same period of 2017 was primarily attributable to our larger clients, driven by an increase in our sales and marketing activities and our improved brand awareness. The adoption of ASC 606 in January 2018 did not have a material impact on the recognition or timing of revenue.

Table of Contents

Cost of Revenue

	Three Months Ended			
	March 31, 2018	March 31, 2017	$ Change	% Change
	(in thousands, except percentages)			
Cost of revenue	$24,702	$19,971	$4,731	24 %
% of Revenue	42 %	42 %		

The increase in cost of revenue for the three months ended March 31, 2018 compared to the same period of 2017 was primarily due to a $2.0 million increase in third party hosted software costs driven by increased client activities and change in timing of the release of deferred cost as required by ASC 340-40 in connection with the adoption of the new revenue standard, a $1.5 million increase in cash-based personnel costs driven mainly by increased headcount, and a $0.6 million increase in USF contributions and other federal telecommunication service fees due primarily to increased client usage.

Gross Profit

	Three Months Ended			
	March 31, 2018	March 31, 2017	$ Change	% Change
	(in thousands, except percentages)			
Gross profit	$34,203	$27,043	$7,160	26 %
% of Revenue	58 %	58 %		

The increase in gross profit for the three months ended March 31, 2018 compared to the same period of 2017 was primarily due to increases in subscription and usage revenues. Gross margin remained consistent for the three months ended March 31, 2018 compared to the same period of 2017.

Operating Expenses

Research and Development

	Three Months Ended			
	March 31, 2018	March 31, 2017	$ Change	% Change
	(in thousands, except percentages)			
Research and development	$7,772	$6,847	$ 925	14 %
% of Revenue	13 %	15 %		

The increase in research and development expenses for the three months ended March 31, 2018 compared to the same period of 2017 was primarily due to a $0.9 million increase in personnel costs including stock-based compensation costs, driven mainly by increased headcount and higher fair value of employee equity awards due primarily to our increased stock price.

Sales and Marketing

	Three Months Ended			
	March 31, 2018	March 31, 2017	$ Change	% Change
	(in thousands, except percentages)			
Sales and marketing	$17,478	$15,778	$1,700	11 %
% of Revenue	30 %	34 %		

The increase in sales and marketing expenses for the three months ended March 31, 2018 compared to the same period of 2017 was primarily due to a $2.0 million increase in personnel-related costs including stock-based compensation costs, driven mainly by increased headcount and higher fair value of employee equity awards due

28

Table of Contents

primarily to our increased stock price, offset in part by a $0.8 million decrease in sales commission expense resulting from the adoption of the new accounting guidance in January 2018. The new accounting guidance requires us to capitalize incremental costs of obtaining contracts with customers consisting primarily of sales commissions. Accordingly, our sales commission expense for the first quarter of 2018 decreased by approximately $1.7 million. See Note 2 for additional information. These increases, as well as the remainder of the increased sales and marketing expenses, were primarily due to the execution of our growth strategy to acquire new clients, to increase the number of agent seats within our existing client base, and to establish brand awareness.

General and Administrative

	Three Months Ended March 31, 2018	March 31, 2017	$ Change	% Change
	(in thousands, except percentages)			
General and administrative	$ 9,103	$ 8,860	$ 243	3 %
% of Revenue	15 %	18 %		

The increase in general and administrative expenses for the three months ended March 31, 2018 compared to the same period of 2017 was primarily due to a $1.3 million increase in stock-based compensation costs mainly due to higher fair value of employee equity awards driven by our increased stock price, a $0.6 million increase in cash-based personnel-related costs driven by increased headcount, offset in part by a $1.8 million settlement and legal costs incurred in the first quarter of 2017.

Other Income (Expense), Net

	Three Months Ended March 31, 2018	March 31, 2017	$ Change	% Change
	(in thousands, except percentages)			
Interest expense	$ (810)	$ (882)	$ 72	8 %
Interest income and other	398	118	280	237 %
Total other income (expense), net	$ (412)	$ (764)	$ 352	46 %
% of Revenue	(1)%	(2)%		

The favorable change in other income (expense), net for the three months ended March 31, 2018 compared to the same period of 2017 was primarily due to a $0.3 million gain from the sale of our convertible notes held for investment. See Note 3 for additional information.

Liquidity and Capital Resources

To date, we have financed our operations primarily through sales of our solution, lease facilities and net proceeds from our equity and debt financings. As of March 31, 2018, we had cash and cash equivalents totaling $80.7 million. As of March 31, 2018, we had a total of $32.6 million outstanding under the Revolving Credit Facility governed by our 2016 Loan and Security Agreement as described below. On August 1, 2016, we entered into a loan agreement (“2016 Loan and Security Agreement”) with two lenders for a new revolving credit facility (“Revolving Credit Facility”) of up to $50.0 million. The Revolving Credit Facility matures on August 1, 2019. Under the terms of the Revolving Credit Facility, the balance outstanding cannot exceed our trailing four months of MRR (monthly recurring revenue including subscription and usage) multiplied by the average trailing 12 month dollar based retention rate (calculated on the same basis as described above under the heading “Annual Dollar-Based Retention Rate”). The Revolving Credit Facility carries a variable annual interest rate of the prime rate plus 0.50%, subject to a 0.25% increase if our adjusted EBITDA is negative at the end of any fiscal quarter. As of March 31, 2018, the amount available for additional borrowings was $17.4 million.

We believe our existing cash and cash equivalents and the amount available for borrowing under our Revolving Credit Facility (or any refinancing of the facility) will be sufficient to meet our working capital and capital expenditure needs for at least the next 12 months. Our future capital requirements will depend on many factors including our

Table of Contents

growth rate, continuing market acceptance of our solution, client retention, our ability to gain new clients, the timing and extent of spending to support development efforts, the outcome of any pending or future litigation or other claims by third parties or governmental entities, the expansion of sales and marketing activities and the introduction of new and enhanced offerings. We may also acquire or invest in complementary businesses, technologies and intellectual property rights, which may increase our future capital requirements, both to pay acquisition costs and to support our combined operations. We may raise additional equity or debt financing at any time. We may not be able to raise additional equity or debt financing on terms acceptable to us or at all. If we are unable to raise additional capital when desired or required, our business, operating results, and financial condition would be harmed. In addition, if our operating performance during the next twelve months is below our expectations, our liquidity and ability to operate our business could be harmed

If we raise additional funds by issuing equity or equity-linked securities, the ownership of our existing stockholders will be diluted. If we raise additional funds through the incurrence of additional indebtedness, we will be subject to increased debt service obligations and could also be subject to new or additional restrictive covenants and other operating restrictions that could harm our ability to conduct our business.

Cash Flows

The following table summarizes our cash flows for the periods presented (in thousands, except percentages):

	Three Months Ended			
	March 31, 2018	March 31, 2017	$ Change	% Change
Net cash provided by operating activities	$7,997	$159	$7,838	4,930 %
Net cash provided by (used in) investing activities	1,490	(514)	2,004	390 %
Net cash provided by (used in) financing activities	2,242	(1,315)	3,557	270 %
Net increase (decrease) in cash and cash equivalents	$11,729	$(1,670)	$13,399	802 %

Cash Flows from Operating Activities

Cash provided by or used in operating activities is primarily influenced by our personnel-related expenditures, data center and telecommunications carrier costs, office and facility related costs, USF contributions and other regulatory costs and the amount and timing of client payments. If we continue to improve our financial results, we expect net cash provided by operating activities to increase. Our largest source of operating cash inflows is cash collections from our clients for subscription and related usage services. Payments from clients for these services are typically received monthly.

During the three months ended March 31, 2018, net cash provided by operating activities was $8.0 million compared to $0.2 million for the same period of 2017. The increase was due to a $6.8 million favorable impact from a decrease in net loss after adjusting for non-cash expenses and a $1.0 million favorable change in net cash flows from operating assets and liabilities.

During the three months ended March 31, 2018, cash inflows from changes in operating assets and liabilities was $1.2 million compared to $0.2 million for the same period of 2017, resulted in an overall improvement of $1.0 million. This improvement was primarily due to a favorable change of $2.1 million in accounts receivable attributed to increased collections from clients and $1.3 million in accounts payable due to timing of payments, offset in part by an unfavorable change of $1.7 million in deferred contract acquisition costs due to the deferral of incremental sales commissions as required by the new accounting guidance in connection with the adoption of ASC 606, and $0.8 million in deferred revenue primarily driven by the adoption of ASC 606. See Note 2 for more information on the adoption impact of ASC 606.

Cash Flows from Investing Activities

Net cash provided by investing activities was $1.5 million for the three months ended March 31, 2018 compared to net cash used $0.5 million for the same period in 2017. The favorable change was primarily driven by the $1.9 million cash proceeds from the sale of our investment during the three months ended March 31, 2018. See Note 3. Our most significant capital expenditures have been investments in our software and equipment for our data centers. We expect such capital investment will continue in the future.

Table of Contents

Cash Flows from Financing Activities

Net cash provided by financing activities was $2.2 million for the three months ended March 31, 2018 compared to net cash used of $1.3 million for the same period in 2017. This favorable change was primarily driven by a $4.0 million increase in cash received from stock option exercises during the three months ended March 31, 2018.

Critical Accounting Policies and Estimates

Our condensed consolidated financial statements are prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses and related disclosures. On an ongoing basis, we evaluate our estimates and assumptions. Our actual results may differ from these estimates under different assumptions or conditions.

We believe our critical accounting policies involve the greatest degree of judgment and complexity and have the greatest potential impact on our condensed consolidated financial statements.

Revenue Recognition

Revenue is recognized when control of the promised services are transferred to customers, in an amount that reflects the consideration that we expect to receive in exchange for those services. We generate all of our revenue from contracts with customers. In contracts with multiple performance obligations, we identify each performance obligation and evaluate whether the performance obligations are distinct within the context of the contract at contract inception. Performance obligations that are not distinct at contract inception are combined. We allocate the transaction price to each distinct performance obligation proportionately based on the estimated standalone selling price for each performance obligation. We then look to how services are transferred to the customer in order to determine the timing of revenue recognition. Most services provided under our agreements result in the transfer of control over time.

Our revenue consists of subscription services and related usage as well as professional services. We charge clients subscription fees, usually billed on a monthly basis, for access to our VCC solution. The monthly subscription fees are primarily based on the number of agent seats, as well as the specific VCC functionalities and applications deployed by the client. Agent seats are defined as the maximum number of named agents allowed to concurrently access the VCC cloud platform. Clients typically have more named agents than agent seats. Multiple named agents may use an agent seat, though not simultaneously. Substantially all of our clients purchase both subscriptions and related telephony usage. A small percentage of our clients subscribe to our platform but purchase telephony usage directly from a wholesale telecommunications service provider. We do not sell telephony usage on a stand-alone basis to any client. The related usage fees are based on the volume of minutes used for inbound and outbound client interactions. We also offer bundled plans, generally for smaller deployments, whereby the client is charged a single monthly fixed fee per agent seat that includes both subscription and unlimited usage in the contiguous 48 states and, in some cases, Canada. Professional services revenue is derived primarily from VCC implementations, including application configuration, system integration, optimization, education and training services. Clients are not permitted to take possession of our software.

We offer monthly, annual and multiple-year contracts to our clients, generally with 30 days' notice required for changes in the number of agent seats and sometimes with a minimum number of agent seats required. Larger clients typically choose annual contracts, which generally include an implementation and ramp period of several months. Fixed subscription fees (including bundled plans) are generally billed monthly in advance, while related usage fees are billed in arrears. Support activities include technical assistance for our solution and upgrades and enhancements to the VCC cloud platform on a when-and-if-available basis, which are not billed separately.

Professional services are primarily billed on a fixed-fee basis and are performed by us directly or, alternatively, clients may also choose to perform these services themselves or engage their own third-party service providers.

The estimation of variable consideration for each performance obligation requires us to make some subjective judgments. In the early stages of our larger contracts, we must estimate variable consideration to be included in the transaction fee, to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved, in order to allocate the overall transaction fee on a relative stand-alone selling price basis to our multiple

31

Table of Contents

performance obligations. This requires the estimate of unit quantities, especially during the initial ramp period of the contract, during which we bill under an ‘actual usage’ model for subscription-related services.

We recognize revenue on fixed fee professional services performance obligations based on the proportion of labor hours expended compared to the total hours expected to complete the related performance obligation.

The revenue recognition standards include guidance relating to any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer and may include, but is not limited to, sales, use, value added and excise taxes. We record USF contributions and other regulatory costs on a gross basis in our condensed consolidated statements of operations and comprehensive loss and record surcharges and sales, use and excise taxes billed to our clients on a net basis. The cost of gross USF contributions payable to the USAC and suppliers is presented as a cost of revenue in the condensed consolidated statements of operations and comprehensive loss.

Recent Accounting Pronouncements

Refer to Note 1 of the notes to condensed consolidated financial statements included in this report.

Off Balance Sheet Arrangements

As of March 31, 2018, we did not have any off balance sheet arrangements, as defined in Item 303(a)(4)(ii) of SEC Regulation S-K, such as the use of unconsolidated subsidiaries, structured finance, special purpose entities or variable interest entities.

Contractual Obligations

Our principal contractual obligations consist of future payment obligations under capital leases to finance data centers and other computer and networking equipment, debt agreements (see Note 6), operating leases agreements for office space, research and development, and sales and marketing facilities, and agreements with third parties to provide co-location hosting, telecommunication usage and equipment maintenance services. These commitments as of December 31, 2017 are disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017, and did not change materially during the three months ended March 31, 2018 except for the acquisition of certain additional data center and network equipment and software under multiple capital leases and certain hosting and telecommunications agreements. As of March 31, 2018, the total minimum future payment commitments under these capital leases added during the three months ended March 31, 2018 were approximately $3.7 million, of which $1.1 million is due during the remainder of 2018, with the remaining $2.6 million due in 2019 to 2021.

During the three months ended March 31, 2018, we entered into various hosting and telecommunications agreements for terms of 12 to 36 months commencing on various dates in 2018. These agreements require us to make monthly payments over the service term in exchange for certain network services. Our total minimum future payment commitments under these agreements are $2.1 million.

Table of Contents

ITEM 3. Quantitative and Qualitative Disclosure about Market Risk

We are exposed to market risk in the ordinary course of our business. Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily a result of fluctuations in interest rates and foreign currency exchange rates. We do not hold or issue financial instruments for trading purposes. For a discussion of market risk, see "Quantitative and Qualitative Disclosure about Market Risk" in Item 7A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2017. Our exposure to market risk has not changed materially since December 31, 2017.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Interim Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of March 31, 2018.

Based on management's evaluation, our Interim Chief Executive Officer and Chief Financial Officer concluded that, as of March 31, 2018, our disclosure controls and procedures were designed, and were effective, to provide assurance at a reasonable level that the information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms, and that such information is accumulated and communicated to our management as appropriate to allow timely decisions regarding required disclosures.

In designing and evaluating our disclosure controls and procedures, management recognizes that any disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Changes in Internal Control over Financial Reporting

Beginning January 1, 2018, we implemented ASU 2014-09, Revenue from Contracts with Customers. We implemented changes to our processes and control activities related to commission expense capitalization and amortization. Although the new standard is expected to have an immaterial impact on our ongoing revenue, we also implemented changes to our processes and control activities addressing the five-step model provided in the new revenue standard and the new disclosure requirements. The new process and control activities implemented include new training, ongoing contract review requirements, and controls around information used in disclosures.

Table of Contents

PART II. OTHER INFORMATION
ITEM 1. Legal Proceedings
Information with respect to this Item may be found under the heading “Legal Matters” in Note 10 of the Notes to Condensed Consolidated Financial Statements in this Quarterly Report on Form 10-Q, which information is incorporated herein by reference.
ITEM 1A. Risk Factors
Our operations and financial results are subject to various risks and uncertainties. You should consider carefully the risks and uncertainties described below, together with all of the other information in this report. If any of the following risks or other risks actually occur, our business, financial condition, results of operations, and future prospects could be materially harmed, and the price of our common stock could decline.
The following description of the risk factors associated with our business includes any material changes to and supersedes the description of the risk factors associated with our business previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2017.
Risks Related to Our Business and Industry
Our quarterly and annual results may fluctuate significantly, may not fully reflect the underlying performance of our business and may result in decreases in the price of our common stock.
Our quarterly and annual results of operations, including our revenues, profitability and cash flow have varied, and may vary significantly in the future, and period-to-period comparisons of our operating results may not be meaningful. Accordingly, the results of any one quarter or period should not be relied upon as an indication of future performance. Our quarterly and annual financial results may fluctuate as a result of a variety of factors, many of which are outside our control and, as a result, may not fully reflect the underlying performance of our business. Fluctuation in quarterly and annual results may harm the value of our common stock. Factors that may cause fluctuations in our quarterly and annual results include, without limitation:

- market acceptance of our solution;
- our ability to attract new clients and grow our business with existing clients;
- client renewal rates;
- our ability to adequately expand our sales and service team;
- our ability to acquire and maintain strategic and client relationships;
- the amount and timing of costs and expenses related to the maintenance and expansion of our business, operations and infrastructure;
- the timing and success of new product and feature introductions by us or our competitors or any other change in the competitive dynamics of our industry, including consolidation among competitors, clients or strategic partners;
- network outages or security incidents, which may result in additional expenses or losses, the loss of clients, the provision of client credits, and harm to our reputation;
- seasonal factors that may cause our revenues in the first half of a year to be relatively lower than our revenues in the second half of a year;
- inaccessibility or failure of our cloud contact center software due to failures in the products or services provided by third parties;
- our ability to expand, and effectively utilize our network of master agents and resellers;
- the timing of recognition of revenues under current and future GAAP;
- changes in our pricing policies or those of our competitors;
- the level of professional services and support we provide our clients;
- the components of our revenue;
- the addition or loss of key clients, including through acquisitions or consolidations;
- general economic, industry and market conditions;

- the timing of costs and expenses related to the development or acquisition of technologies or businesses and potential future charges for impairment of goodwill from acquired companies;
- compliance with, or changes in, the current and future domestic and international regulatory environment;
- the hiring, training and retention of key employees;
- litigation or other claims against us;
- the ability to expand internationally, and to do so profitability;
- our ability to obtain additional financing;
- advances and trends in new technologies and industry standards; and
- increases or decreases in the costs to provide our solution or pricing changes upon any renewals of client agreements.

If we are unable to attract new clients or sell additional services and functionality to our existing clients, our revenue and revenue growth will be harmed.

To increase our revenue, we must add new clients, add additional agent seats and sell additional functionality to existing clients, and encourage existing clients to renew their subscriptions on terms favorable to us. As our industry matures, as our clients experience seasonal trends in their business, or as competitors introduce lower cost or differentiated products or services that are perceived to compete favorably with ours, our ability to add new clients and renew, maintain or sell additional services to existing clients based on pricing, cost of ownership, technology and functionality could be harmed. As a result, our existing clients may not renew our agreements or may decrease the number of agent seats, and we may be unable to attract new clients or grow or maintain our business with existing clients, which could harm our revenue and growth.

Furthermore, a portion of our revenue is generated by acquiring domestic and international telecommunications minutes from wholesale telecommunication service providers and reselling those minutes to our clients. As a result, if telecommunications rates decrease, we must resell more minutes to maintain our level of usage revenue.

Our recent rapid growth may not be indicative of our future growth, and if we continue to grow rapidly, we may fail to manage our growth effectively.

For the three months ended March 31, 2018, our revenue was $58.9 million, which increased by $11.9 million, or 25%, from $47.0 million for the same period of 2017. For the years ended December 31, 2017, 2016 and 2015, our revenues were $200.2 million, $162.1 million, and $128.9 million, respectively, representing year-over-year growth of 24% and 26%, respectively. In the future, as our revenue increases, our quarterly or annual revenue growth rate may decline. We believe our revenue growth will depend on a number of factors, including our ability to:

- compete with other vendors of cloud-based enterprise contact center systems to capture market share, including from providers of legacy on-premise systems;
- increase our existing clients' use of our solution and further develop our partner ecosystem;
- strengthen and improve our solution through significant investments in research and development and the introduction of new and enhanced solutions;
- introduce our solution to new markets outside of the United States and increase global awareness of our brand; and
- selectively pursue acquisitions.

If we are not successful in achieving these objectives, our ability to grow our revenue may be negatively impacted. In addition, we plan to continue to invest in future growth, including expending substantial financial and other resources on:

- sales and marketing, including a significant expansion of our sales and professional services organization;
- our technology infrastructure, including systems architecture, management tools, scalability, availability, performance and security, as well as disaster recovery measures;
- solution development, including investments in our solution development team and the development of new solutions, as well as new applications and features for existing solutions;
- international expansion; and

Table of Contents

- general administration, including legal, regulatory compliance and accounting expenses.

Moreover, we continue to expand our headcount and operations. We grew from 807 employees as of March 31, 2017 to 873 employees as of March 31, 2018. We anticipate that we will continue to expand our operations and headcount in the near term. This growth has placed, and future growth will place, a significant strain on our management, administrative, operational and financial resources and infrastructure. Our success will depend in part on our ability to manage this growth effectively. To manage the expected growth of our operations and personnel, we will need to continue to improve our operational, financial and management controls and our reporting systems and procedures. Failure to effectively manage growth could result in difficulty or delays in adding new clients, declines in quality or client satisfaction, increases in costs, system failures, difficulties in introducing new features or solutions, the need for more capital than we anticipate or other operational difficulties, and any of these difficulties could harm our business performance and results of operations.

The expected addition of new employees and the capital investments that we anticipate will be necessary to manage our growth will make it more difficult for us to generate earnings or offset any future revenue shortfalls by reducing costs and expenses in the short term. If we fail to manage our anticipated growth, we will be unable to execute our business plan successfully.

Failure to adequately expand our direct sales force will impede our growth.

We need to continue to expand and optimize our sales infrastructure in order to grow our client base and business. We plan to continue to expand our direct sales force, both domestically and internationally. Identifying and recruiting qualified personnel and training them in the use and sale of our solution requires significant time, expense and attention. It can take several months before our sales representatives are fully trained and productive. Our business may be harmed if our efforts, and the expense incurred, to expand and train our direct sales force do not generate a corresponding increase in revenues. In particular, if we are unable to hire, develop and retain talented sales personnel or if new sales personnel are unable to achieve desired productivity levels in a reasonable period of time, we may not be able to realize the expected benefits of this investment or increase our revenues.

If we fail to manage our technical operations infrastructure, our existing clients may experience service outages, our new clients may experience delays in the deployment of our solution and we could be subject to, among other things, claims for credits or damages.

Our success depends in large part upon the capacity, stability and performance of our operations infrastructure. From time to time, we have experienced interruptions in service, and may experience such interruptions in the future. These service interruptions may be caused by a variety of factors, including infrastructure changes, human or software errors, viruses, security attacks, fraud, spikes in client usage and denial of service issues. In some instances, we may not be able to identify the cause or causes of these performance problems within an acceptable period of time. Our failure to achieve or maintain expected performance levels, stability and security could harm our relationships with our clients, result in claims for credits or damages, damage our reputation and significantly reduce client demand for our solution and harm our business.

Any future service interruptions could:

- cause our clients to seek credits or damages for losses incurred;
- cause existing clients to cancel their contracts and move to a competitor;
- affect our reputation as a reliable service provider;
- make it more difficult for us to attract new clients or expand our business with existing clients; or
- require us to replace existing equipment.

We have experienced significant growth in the number of agents and interactions that our infrastructure supports. As the number of agent seats within our client base grows and our clients' use of our service increases, we need to continue to make additional investments in our capacity to maintain adequate stability and performance, the availability of which may be limited or the cost of which may be prohibitive. In addition, we need to properly manage our operations infrastructure in order to support version control, changes in hardware and software parameters and the evolution of our solution. If we do not accurately predict or improve our infrastructure requirements to keep pace with growth in our business, our business could be harmed.

36

Table of Contents

Security breaches and improper access to or disclosure of our data or our clients' data, or other cyber attacks on our systems, could result in litigation and regulatory risk, harm our reputation and adversely affect our business.

Our solution involves the storage and transmission of our clients' information, including information about our clients' customers or other information treated by our clients as confidential. Unauthorized access, unauthorized use of our systems, security breaches or other cyber attacks could result in the loss of confidentiality, integrity and availability of such information, leading to litigation, indemnity obligations, increased expense, and other liability. Such incidents could also cause interruptions to the solution we provide, degrade the user experience, or cause clients to lose confidence in our solution. In April 2017, we were notified that third parties were suspected of having unlawfully acquired some of our clients' information. We conducted an investigation, believe this acquisition was the result of a vulnerability that has now been remediated, and notified clients we determined may have been impacted. Expenses related to this incident were not material.

While we have security measures in place to protect client information and minimize the probability of security breaches and other cyber attacks, if these measures fail as a result of a cyber-attack, other third-party action, employee error, malfeasance or otherwise, and someone obtains unauthorized access to our clients' information, our reputation could be damaged, our business may suffer and we could incur significant liability. Because the techniques used to obtain unauthorized access or sabotage systems change frequently and generally are not identified until they are launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. In addition, third parties may attempt to fraudulently induce employees or users to disclose information in order to gain access to our data or our users' data. Moreover, any failure on the part of third parties, including our clients, to maintain appropriate security measures for their own systems could harm our relationships with our clients, result in claims against us for credits or damages, damage our reputation and significantly reduce client demand for our solution. Any or all of these issues could harm our ability to attract new clients, cause existing clients to cancel, reduce or not renew their subscriptions, result in reputational damage or subject us to third-party lawsuits, regulatory fines or other action or liability, including orders or consent decrees forcing us to modify our business practices, all of which could have a material and adverse effect on our business, reputation or financial results.

The markets in which we participate are highly competitive, and if we do not compete effectively, our operating results could be harmed.

The market for contact center solutions is highly competitive. Generally, we do not have long-term contracts with our clients and our clients can terminate our service and switch to competitors' offerings on short notice.

We currently compete with large legacy technology vendors that offer on-premise enterprise telephony and contact center systems, such as Avaya and Cisco, and legacy on-premise software companies that come from a computer-telephony integration, or CTI, heritage, such as Aspect and Genesys (including through its acquisition of Interactive Intelligence). These companies are supplementing their traditional on-premise contact center systems with cloud offerings, either through acquisition or in-house development. Additionally, we compete with vendors that historically provided other contact center services and technologies and expanded to offer cloud contact center software. These companies include inContact (acquired by NICE Ltd.) and LiveOps, now named Seranova. We also face competition from smaller contact center service providers with specialized contact center software offerings. Our actual and potential competitors may enjoy competitive advantages over us, including greater name recognition, longer operating histories and larger marketing budgets, as well as greater financial or technical resources. With the introduction of new technologies and market entrants, we expect competition to intensify in the future.

Some of our competitors can devote significantly greater resources than we can to the development, promotion and sale of their products and services and many have the ability to initiate or withstand substantial price competition. Current or potential competitors may also be acquired by third parties with significantly greater resources, such as NICE Ltd.'s acquisition of inContact and Genesys' acquisition of Interactive Intelligence. In addition, many of our competitors have stronger name recognition, longer operating histories, established relationships with clients, more comprehensive product offerings, larger installed bases and major distribution agreements with consultants, system integrators and resellers. Our competitors may also establish cooperative relationships among themselves or with third parties that may further enhance their product offerings or resources and ability to compete. If our competitors' products, services or technologies become more accepted than our solution, if they are successful in bringing their products or services to market earlier than ours, or if their products or services are less expensive or more technologically capable than ours, our revenues could be harmed. Pricing pressures and increased competition could result in reduced sales and revenues, reduced margins and loss of, or a failure to maintain or improve, our competitive market position, any of which could harm our business.

If our existing clients terminate their subscriptions or reduce their subscriptions and related usage, our revenues and gross margins will be harmed and we will be required to spend more money to grow our client base.

We expect to continue to derive a significant portion of our revenues from existing clients. As a result, retaining our existing clients is critical to our future operating results. We offer monthly, annual and multiple-year contracts to our clients, with 30 days' notice generally required for changes in the number of agent seats, including to zero, or termination of their contracts. Subscriptions and related usage by our existing clients may decrease if:

- clients are not satisfied with our services, prices or the functionality of our solution;
- the stability, performance or security of our solution are not satisfactory;
- our clients' business declines due to industry cycles, seasonality, business difficulties or other reasons;
- competition increases from other contact center providers;
- fewer clients purchase usage from us;
- alternative technologies, products or features emerge that we do not provide;
- our clients or potential clients experience financial difficulties; or
- the U.S. or global economy declines.

If our existing clients' subscriptions and related usage decrease or are terminated, we will need to spend more money to acquire new clients to maintain our existing level of revenues. We incur significant costs and expenses, including sales and marketing expenses, to acquire new clients, and those costs and expenses are an important factor in determining our net profitability. There can be no assurance that our efforts to acquire new clients will be successful.

Our growth depends in part on the success of our strategic relationships with third parties and our failure to successfully grow and manage these relationships could harm our business.

We leverage strategic relationships with third parties, such as customer relationship management, or CRM, providers, Workforce Optimization, or WFO, providers, other technology providers, system integrators, and telephony providers. For example, our CRM and system integrator relationships provide significant lead generation for new client opportunities. These relationships are typically not exclusive and our partners often also offer products of our competitors. As we grow our business, we will continue to depend on both existing and new strategic relationships. Our competitors may be more successful than we are in establishing or expanding relationships with third parties or may provide incentives to third parties to favor their products over our solution. These strategic partners may cease to recommend our solution to prospective clients due to actual or perceived lack of features, technological or security issues or failures, reputational concerns, economic incentives, or other factors, which would harm our business, financial condition and operations. Furthermore, there has and continues to be a significant amount of consolidation in our industry and adjacent industries, and if our partners are acquired, fail to work effectively with us or go out of business, they may no longer support or promote our solution, or may be less effective in doing so, which could harm our business, financial condition and operations. If we are unsuccessful in establishing or maintaining our strategic relationships with third parties, or these partners fail to recommend our solution, our ability to compete in the marketplace or to grow our revenues could be impaired and our operating results may suffer. Even if we are successful, we cannot assure you that these relationships will result in increased client usage of our solution or increased revenue.

In addition, identifying new partners, and negotiating and documenting relationships with them, requires significant time and resources. As the complexity of our solution and our third-party relationships increases, the management of those relationships and the negotiation of contractual terms sufficient to protect our rights and limit our potential liabilities will become more complicated. We also license technology from certain third parties, including through OEM relationships. Certain of these agreements permit either party to terminate all or a portion of the relationship without cause at any time and for any reason. If one of these agreements is terminated by the other party, we would have to find an alternative source or develop new technology ourselves, either of which could cause delays in our ability to offer our solution or certain product features to our clients, result in increased expense and harm our business. Our inability to successfully manage and maintain these complex relationships or negotiate sufficient contractual terms could harm our business.

Table of Contents

We are establishing a network of master agents and resellers to sell our solution; our failure to effectively develop, manage, and maintain this network could materially harm our revenues.

We are establishing a network of master sales agents, which provide sales leads, and resellers, which sell our solution to new and existing clients. We expect that this network will enable us to attract additional clients. We expect our resellers will also assist us in expanding internationally. These master agents and resellers sell, or may in the future decide to sell, solutions for our competitors. Our competitors may be able to cause our current or potential master agents or resellers to favor their services over ours, either through financial incentives, technological innovation, by offering a broader array of services to these service providers or otherwise, which could reduce the effectiveness of our use of these third parties. If we fail to maintain relationships with current master agents and resellers, fail to develop relationships with new master agents and resellers in new and existing markets, if we fail to manage, train, or provide appropriate incentives to our existing master agents and resellers, or if our master agents and resellers are not successful in their sales efforts, sales of our subscriptions may decrease or not grow at an appropriate rate and our operating results could be harmed.

In addition, identifying new resellers, and negotiating and documenting relationships with them, requires significant time and resources. As the complexity of our solution and our reseller relationships increases, the management of those relationships and the negotiation of contractual terms sufficient to protect our rights and limit our potential liabilities will become more complicated. Our inability to successfully manage these complex relationships or negotiate sufficient contractual terms could harm our business.

The loss of one or more of our key clients, or a failure to renew our subscription agreements with one or more of our key clients, could harm our ability to market our solution.

We rely on our reputation and recommendations from key clients in order to market and sell our solution. The loss of any of our key clients, or a failure of some of them to renew or to continue to recommend our solution, could have a significant impact on our revenues, reputation and our ability to obtain new clients. In addition, acquisitions of our clients could lead to cancellation of our contracts with those clients, thereby reducing the number of our existing and potential clients.

Our clients may fail to comply with the terms of their agreements, necessitating action by us to collect payment, or may terminate their subscriptions for our solution.

If clients fail to pay us under the terms of our agreements or fail to comply with the terms of our agreements, including compliance with regulatory requirements, we may terminate clients, lose revenue, be unable to collect amounts due to us, be subject to legal or regulatory action and incur costs in enforcing the terms of our contracts, including litigation. Some of our clients may seek bankruptcy protection or other similar relief and fail to pay amounts due to us, seek reimbursement for amounts already paid, or pay those amounts more slowly, either of which could harm our operating results, financial position and cash flow.

We sell our solution to larger organizations that require longer sales and implementation cycles and often demand more configuration and integration services or customized features and functions that we may not offer, any of which could delay or prevent these sales and harm our growth rates, business and operating results.

As we continue to target our sales efforts at larger organizations, we face greater costs, longer sales and implementation cycles and less predictability in closing sales. These larger organizations typically require more configuration and integration services, which increases our upfront investment in sales and deployment efforts, with no guarantee that these clients will subscribe to our solution or increase the scope of their subscription. Furthermore, with larger organizations, we must provide greater levels of education regarding the use and benefits of our solution to a broader group of people. As a result of these factors, we must devote a significant amount of sales support and professional services resources to individual clients and prospective clients, thereby increasing the cost and time required to complete sales. Our typical sales cycle for larger organizations is four to six months, but can be significantly longer, and we expect that our average sales cycle may increase as sales to larger organizations continue to grow as a percentage of our business. Longer sales cycles could cause our operating and financial results to be less predictable and to fluctuate from period to period. In addition, many of our clients that are larger organizations initially deploy our solution to support only a portion of their contact center agents. Our success depends on our ability to increase the number of agent seats and the number of applications utilized by larger organizations over time. There is no guarantee that these clients will increase their subscriptions for our solution. If we do not expand our initial relationships with larger organizations, the return on our investments in sales and deployment efforts for these clients will decrease and our business may suffer.

Table of Contents

Furthermore, we may not be able to provide the configuration and integration services that larger organizations typically require. For example, our solution does not currently permit clients to modify our software code, but instead requires them to use our set of application programming interfaces, or APIs. If prospective clients require customized features or functions that we do not offer, and that would be difficult for them to deploy themselves, they will need to use our services or third-party service providers or we may lose sales opportunities with larger organizations and our business could suffer.

Because a significant percentage of our revenue is derived from existing clients, downturns or upturns in new sales will not be immediately reflected in our operating results and may be difficult to discern.

We generally recognize subscription revenue from clients monthly as services are delivered. As a result, a significant percentage of the subscription revenue we report in each quarter is derived from existing clients. Consequently, a decline in new subscriptions in any single quarter will likely have only a small impact on our revenue results for that quarter. However, the cumulative impact of such declines could negatively impact our business and results of operations in future quarters. Accordingly, the effect of significant downturns in sales and market acceptance of our solution, and potential changes in our pricing policies or renewal rates, will typically not be reflected in our results of operations until future periods. We also may be unable to adjust our cost structure to reflect the changes in revenue, resulting in lower margins and earnings. In addition, our subscription model makes it difficult for us to rapidly increase our revenue through additional sales in any period, as revenue from new clients will be recognized over time as services are delivered. For example, many of our clients initially deploy our solution to support only a portion of their contact center agents. Any increase to our revenue and the value of these existing client relationships will only be reflected in our results of operations if and when these clients increase the number of agent seats and the number of components of our solution over time.

We rely on third-party telecommunications and internet service providers to provide our clients and their customers with telecommunication services and connectivity to our cloud contact center software and any failure by these service providers to provide reliable services could cause us to lose clients and subject us to claims for credits or damages, among other things.

We rely on third-party telecommunication service providers to provide our clients and their customers with telecommunication services. These telephony services include the public switched telephone network, or PSTN, telephone numbers, call termination and origination services, and local number portability for our clients. In addition, we depend on our internet bandwidth suppliers to provide uninterrupted and error-free service through their telecommunications networks. We exercise little control over these third-party providers, which increases our vulnerability to problems with the services they provide.

When problems occur, it may be difficult to identify the source of the problem. Service disruption or outages, whether caused by our service, the products or services of our third-party service providers, or our clients' or their customers' equipment and systems, may result in loss of market acceptance of our solution and any necessary repairs or other remedial actions may force us to incur significant costs and expenses.

If any of these service providers fail to provide reliable services, suffer outages, degrade, disrupt, increase the cost of or terminate the services that we and our clients depend on, we may be required to switch to another service provider. Delays caused by switching our technology to another service provider, if available, and qualifying this new service provider could materially harm our client relationships, business, financial condition and operating results. Further, any failure on the part of third-party service providers to achieve or maintain expected performance levels, stability and security could harm our relationships with our clients, cause us to lose clients, result in claims for credits or damages, increase our costs or the costs incurred by our customers, damage our reputation, significantly reduce client demand for our solution and seriously harm our financial condition and operating results.

Our clients and their customers rely on internet service providers to provide them with access and connectivity to our cloud contact center software and changes in how internet service providers handle and charge for access to the internet could materially harm our client relationships, business, financial condition and operations results.

In 2015, the FCC released an order, commonly referred to as net neutrality, that, among other things, prohibited (i) the impairment or degradation of lawful internet traffic on the basis of content, application or service and (ii) the practice of favoring some internet traffic over other internet traffic based on the payment of higher fees. In December 2017, the FCC voted to overturn the net neutrality regulations imposed by the 2015 order. Internet service providers in the U.S. may now be able to impair or degrade the use of, or increase the cost of using, our solution. Net neutrality regulations vary widely among the jurisdictions in which we operate. While certain

Table of Contents

jurisdictions have strong protections for services such as ours, other countries either lack a net neutrality framework or otherwise do not strictly enforce net neutrality regulations. The impairment, degradation or prioritization of lawful internet traffic by internet service providers could materially harm our client relationships, business, financial condition and operating results.

We depend on data centers operated by third parties and any disruption in the operation of these facilities could harm our business.

We host our solution at data centers located in Santa Clara, California; Atlanta, Georgia; Slough, England and Amsterdam, the Netherlands. Any failure or downtime in one of our data center facilities could affect a significant percentage of our clients. While we control and have access to our servers and all of the components of our network that are located in our external data centers, we do not control the operation of these facilities. The owners of our data center facilities have no obligation to renew their agreements with us on commercially reasonable terms, or at all. If we are unable to renew these agreements on commercially reasonable terms, or if one of our data center operators is acquired, closes, suffers financial difficulty or is unable to meet our growing capacity needs, we may be required to transfer our servers and other infrastructure to new data center facilities, and we may incur significant costs and service interruptions in connection with doing so.

Our data centers are subject to various points of failure. Problems with cooling equipment, generators, uninterruptible power supply, routers, switches, or other equipment, whether or not within our control, could result in service interruptions for our clients as well as equipment damage. Our data centers are subject to disasters such as earthquakes, floods, fires, hurricanes, acts of terrorism, sabotage, break-ins, acts of vandalism and other events, which could cause service interruptions or the operators of these data centers to close their facilities for an extended period of time or permanently. The destruction or impairment of any of our data center facilities could result in significant downtime for our solution and the loss of client data. Because our ability to attract and retain clients depends on our providing clients with highly reliable service, even minor interruptions in our service could harm our business, revenues and reputation. Additionally, in connection with the continuing expansion of our existing data center facilities, there is an increased risk that service interruptions may occur as a result of server addition, relocation or other issues.

Our data centers are also subject to increased power costs. We may not be able to pass on any increase in power costs to our clients, which could reduce our operating margins.

Shifts over time or from quarter-to-quarter in the mix of sizes or types of organizations that purchase our solution or changes in the components of our solution purchased by our clients could affect our gross margins and operating results.

Our strategy is to sell our solution to both smaller and larger organizations. Our gross margins can vary depending on numerous factors related to the implementation and use of our solution, including the features and number of agent seats purchased by our clients and the level of usage and professional services and support required by our clients. For example, our larger clients typically require more professional services and because our professional services offerings typically have negative margins, any increase in sales of professional services could harm our gross margins and operating results. We also have lower margins on our usage revenues. Sales to larger organizations may also entail longer sales cycles and more significant selling efforts. Selling to smaller clients may involve smaller contract sizes, fewer opportunities to sell additional services, a higher likelihood of contract terminations, fewer potential agent seats and greater credit risk and uncertainty. If the mix of organizations that purchase our solution, or the mix of solution components purchased by our clients, changes unfavorably, our revenues and gross margins could decrease and our operating results could be harmed.

We are in the process of expanding our international operations, which exposes us to significant risks.

To date, we have not generated significant revenues outside of the U.S., Canada and the U.K. However, we already have significant operations outside these countries and we expect to grow our international presence in the future. The future success of our business will depend, in part, on our ability to expand our operations and customer base to other countries. Operating in international markets requires significant resources and management attention and will subject us to regulatory, economic, and political risks that are different from those in the U.S. Due to our limited experience with international operations and developing and managing sales and distribution channels in international markets, our international expansion efforts may not be successful.

Table of Contents

We have a history of losses and we may be unable to achieve or sustain profitability.
We have incurred significant losses in each period since our inception in 2001, with the exceptions of the three months ended December 31, 2016 and September 30, 2017. We incurred net losses of $0.6 million and 5.3 million in the three months ended March 31, 2018 and 2017, respectively, and a net loss of $9.0 million in the year ended December 31, 2017. As of March 31, 2018, we had an accumulated deficit of $151.9 million. These losses and our accumulated deficit reflect the substantial investments we have made to develop our solution and acquire new clients. We expect the dollar amount of our costs and expenses to increase in the future as revenue increases, although at a slower rate. We expect our losses to continue for the foreseeable future as we continue to develop and expand our business. Furthermore, to the extent we are successful in increasing our client base, we may also incur increased losses because costs associated with acquiring clients are generally incurred up front, while revenues are recognized over the course of the client relationship. We also have negative gross margins on our professional services, which are expected to continue in the medium term. In addition, as a public company, we incur significant legal, accounting and other expenses. Our historical or recent growth in revenues is not necessarily indicative of our future performance. Accordingly, there is no assurance that we will achieve profitability in the future nor that, if we do become profitable, we will sustain profitability.
If the market for cloud contact center software solutions develops more slowly than we expect or declines, our business could be harmed.
The cloud contact center software market is not as mature as the market for legacy on-premise contact center systems, and it is uncertain whether cloud contact center solutions will achieve and sustain high levels of client demand and market acceptance. Our success will depend to a substantial extent on the widespread adoption of cloud contact center software solutions as a replacement for legacy on-premise systems. Many larger organizations have invested substantial technical, personnel and financial resources to integrate legacy on-premise contact center systems into their businesses and, therefore, may be reluctant or unwilling to migrate to cloud contact center solutions such as ours. It is difficult to predict client adoption rates and demand for our solution, the future growth rate and size of the cloud contact center software market, or the entry of competitive products and services. The expansion of the cloud contact center software market depends on a number of factors, including the refresh rate for legacy on-premise systems, cost, performance and perceived value associated with cloud contact center software solutions, as well as the ability of providers of cloud contact center software solutions to address security, stability and privacy concerns. If we or other cloud contact center solution providers experience security incidents, loss of client data, disruptions in service or other problems, the market for cloud contact center software products, solutions and services as a whole, including our solution, may be harmed. If cloud contact center software solutions do not achieve widespread adoption, or there is a reduction in demand for such solutions caused by a lack of client acceptance, enhanced product offerings from on-premise providers, technological challenges, weakening economic conditions, security or privacy concerns, competing technologies and products, decreases in corporate spending or otherwise, it could result in decreased revenues and our business could be harmed.
Our recent growth makes it difficult to evaluate and predict our current business and future prospects.
While we have been in existence since 2001, much of our growth has occurred in recent years. Our recent growth may make it difficult for investors to evaluate our current business and our future prospects. We have encountered and will continue to encounter risks and difficulties frequently experienced by growing companies in rapidly changing industries, including increasing and unforeseen expenses as we continue to grow our business.
Our ability to forecast our future operating results is limited and subject to a number of uncertainties, including our ability to predict revenue levels, and plan for and model future growth. We have encountered and will continue to encounter risks and uncertainties frequently experienced by growing companies in rapidly changing industries, such as the risks and uncertainties described in this report. If our assumptions regarding these risks and uncertainties, which we use to plan our business, are incorrect or change due to adjustments in our markets or our competitors and their product offerings, or if we do not address these risks successfully, our operating and financial results could differ materially from our expectations and our business could suffer.

If our solution fails, or is perceived to fail, to perform properly or if it contains technical defects, our reputation could be harmed, our market share may decline and we could be subject to product liability claims.

Our solution may contain undetected errors or defects that may result in failures or otherwise cause our solution to fail to perform in accordance with client expectations. Moreover, our clients could incorrectly implement or inadvertently misuse our products, which could result in client dissatisfaction and harm the perceived utility of

Table of Contents

our products and our brand. Because our clients use our solution for mission-critical aspects of their business, any real or perceived errors or defects in, or other performance problems with, our solution may damage our clients' businesses and could significantly harm our reputation. If that occurs, we could lose future sales, or our existing clients could elect to cancel our solution, seek payment credits, seek damages against us, or delay or withhold payment to us, which could result in reduced revenues, an increase in our provision for uncollectible accounts and service credits, an increase in collection cycles for accounts receivable, and harm our financial results. In addition, since telecommunications billing is inherently complex and requires highly sophisticated information systems to administer, our billing system may experience errors or we may improperly operate the system, which could result in the system incorrectly calculating the fees owed by our clients or related taxes and administrative fees. Clients also may make indemnification or warranty claims against us, which could result in significant expense and risk of litigation. Product performance problems could result in loss of market share, failure to achieve market acceptance and the diversion of development resources.

Any product liability, intellectual property, warranty or other claims against us could damage our reputation and relationships with our clients, and could require us to spend significant time and money in litigation or pay significant settlements or damages. Although we maintain general liability insurance, including coverage for errors and omissions, this coverage may not be sufficient to cover liabilities resulting from such claims. Also, our insurers may disclaim coverage. Our liability insurance also may not continue to be available to us on reasonable terms, in sufficient amounts, or at all. Any contract or product liability claims successfully brought against us would harm our business.

We are subject to many hazards and operational risks that can disrupt our business, some of which may not be insured or fully covered by insurance.

Our operations are subject to many hazards inherent in the cloud contact center software business, including:

- damage to third-party and our infrastructure and data centers, related equipment and surrounding properties caused by earthquakes, hurricanes, tornadoes, floods, fires and other natural disasters, explosions and acts of terrorism;
- security breaches resulting in loss or disclosure of confidential client and customer data and potential liability to clients and non-client third parties for such disclosures;
- inadvertent damage from third parties; and
- other hazards that could also result in suspension of operations, personal injury and even loss of life.

These risks could result in substantial losses and the curtailment or suspension of our operations. For example, in the event of a major earthquake along the West Coast of the United States (where our corporate headquarters and one of our data centers are located), hurricane, tropical storm or severe weather in the southeastern United States (where our other U.S. data center is located) or catastrophic events such as fire, power loss, telecommunications failure, cyber-attack, war or terrorist attack, we may be unable to continue our operations and may endure system and service interruptions, reputational harm, delays in product development, breaches of data security and loss of critical data, any of which could harm our business and operating results.

We are not insured against all claims, events or accidents that might occur. If a significant accident or event occurs that is not fully insured, if we fail to recover all anticipated insurance proceeds for significant accidents or events for which we are insured, or if we or our data center providers fail to reopen facilities damaged by such accidents or events, our operations and financial condition could be harmed. In addition to being denied coverage under existing insurance policies, we may not be able to maintain or obtain insurance of the type and amount we desire at reasonable rates.

The contact center software solutions market is subject to rapid technological change, and we must develop and sell incremental and new products in order to maintain and grow our business.

The contact center software solutions market is characterized by rapid changes in client requirements, frequent introductions of new and enhanced products and features and continuing and rapid technological advancement. To compete successfully, we must continue to design, develop, manufacture and sell new and enhanced contact center products, applications and features that provide increasingly higher capabilities, performance and stability at lower cost. If we are unable to develop or acquire new features for our existing solution or new applications that achieve market acceptance or that keep pace with technological developments, our business would be harmed. For example, we are focused on enhancing the reliability, features and functionality of our contact center solution to enhance its

Table of Contents

utility to our clients, particularly larger clients with complex, dynamic and global operations. The success of these enhancements depends on many factors, including timely development, introduction and market acceptance, as well as our ability to transition our existing clients to these new products, applications and features. Failure in this regard may significantly impair our revenue growth. In addition, because our solution is designed to operate on a variety of systems, we will need to continuously modify and enhance our solution to keep pace with changes in hardware, operating systems, the increasing trend toward multi-channel communications and other changes to software technologies. We may not be successful in developing or acquiring these modifications and enhancements or bringing them to market in a timely fashion. Furthermore, uncertainties about the timing and nature of new network platforms or technologies, or modifications to existing platforms or technologies, could delay introduction of our solution and increase our research and development expenses. Any failure of our solution to operate effectively with future network platforms and technologies could reduce the demand for our solution, result in client dissatisfaction and harm our business.

Our ability to continue to enhance our solution is dependent on adequate research and development resources. If we are not able to adequately fund our research and development efforts, we may not be able to compete effectively and our business and operating results may be harmed.

In order to remain competitive, we must continue to develop new solution offerings and enhancements to our existing cloud contact center software. Maintaining adequate research and development personnel and resources to meet the demands of the market is essential. If we are unable to develop products, applications or features internally due to constraints, such as high employee turnover, insufficient cash, inability to hire sufficient research and development personnel or a lack of other research and development resources, we may miss market opportunities. Furthermore, many of our competitors expend considerably greater amounts on their research and development programs than we do, and those that do not may be acquired by larger companies that would allocate greater resources to our competitors' research and development programs. Our failure to devote adequate research and development resources or compete effectively with the research and development programs of our competitors could harm our business.

If we are unable to maintain the compatibility of our software with other products and technologies, our business would be harmed.

Our clients often integrate our solution with their business applications, particularly third-party CRM solutions. These third-party providers or their partners could alter their products so that our solution no longer integrates well with them, or they could delay or deny our access to technology releases that allow us to adapt our solution to integrate with their products in a timely fashion. If we cannot adapt our solution to changes in complementary technology deployed by our clients, it may significantly impair our ability to compete effectively.

Our business could be harmed if our clients are not satisfied with the professional services and technical support provided by us or our partners.

Our business depends on our ability to satisfy our clients, not only with respect to our solution, but also with the professional services and technical support that are required for our clients to implement and use our solution to address their business needs. Professional services and technical support may be performed by our own staff or, in a select subset of cases, by third parties. We will need to continue to expand and optimize our professional services and technical support in order to keep up with new client installations and ongoing service, which will take time and expense to implement. Identifying and recruiting qualified service personnel and training them in our solution is difficult and competitive and requires significant time, expense and attention. We may be unable to respond quickly enough to accommodate short-term increases in client demand for support services. We also may be unable to modify the format of our support services or change our pricing to compete with changes in support services provided by our competitors. Increased client demand for these services, without corresponding revenues, could increase our costs and harm our operating results. If a client is not satisfied with the deployment and ongoing services performed by us or a third party, then we could lose clients, miss opportunities to expand our business with these clients, incur additional costs, or suffer reduced margins on, our service revenue, any of which could damage our ability to grow our business. In addition, negative publicity related to our professional services and technical support, regardless of its accuracy, may damage our business by affecting our ability to compete for new business with current and prospective clients.

Table of Contents

Sales to clients outside the United States or with international operations and our international sales efforts and operations support expose us to risks inherent in international sales and operations.

A key element of our growth strategy is to expand our international sales efforts and develop a worldwide client base. Because of our limited experience with international sales, our international expansion may not be successful and may not produce the return on investment we expect. To date, we have realized only a small portion of our revenues from clients outside the United States.

Our international employees are primarily located in the Philippines, where technical support, training and other professional services are performed, and Russia, where software development services are performed. We have also started to increase our sales, marketing and support personnel in the U.K. to maintain and support our European data centers and to provide service and support to clients in the European Union. Operating in international markets requires significant resources and management attention and subjects us to intellectual property, regulatory, economic and political risks that are different from those in the United States. As we increase our international sales efforts and continue our other international operations, we will face risks in doing business internationally that could harm our business, including:

- the need to establish and protect our brand in international markets;
- the need to localize and adapt our solution for specific countries, including translation into foreign languages and associated costs and expenses;
- difficulties in staffing and managing foreign operations, particularly hiring and training qualified sales and service personnel;
- the need to make implementations, and offer customer care, in various native languages;
- different pricing environments, longer sales and accounts receivable payment cycles and collections issues;
- weaker protection for intellectual property and other legal rights than in the U.S. and practical difficulties in enforcing intellectual property and other rights outside of the U.S.;
- increased risk of piracy, counterfeiting and other misappropriation of our intellectual property in our locations outside the U.S.;
- new and different sources of competition;
- general economic conditions in international markets;
- fluctuations in the value of the U.S. dollar and foreign currencies, which may make our solution more expensive in other countries or may increase our costs, impacting our operating results when translated into U.S. dollars;
- compliance with customs duties, tariffs and other international trade complexities;
- compliance challenges related to the complexity of multiple, conflicting and changing governmental laws and regulations, including employment, tax, telecommunications and telemarketing laws and regulations;
- privacy and data protection laws and regulations that are complex, expensive to comply with and may require that client data be stored and processed in a designated territory;
- increased risk of international telecom fraud;
- laws and business practices favoring local competitors;
- compliance with laws and regulations for foreign operations, including the Foreign Corrupt Practices Act, the U.K. Bribery Act and other anti-corruption laws, import and export control laws, tariffs, trade barriers, economic sanctions and regulatory or contractual limitations on our ability to sell our solution in certain foreign markets, and the risks and costs of non-compliance;
- increased financial accounting and reporting burdens and complexities;
- restrictions or taxes on the transfer of funds;
- adverse tax consequences; and
- unstable economic and political conditions.

These risks could harm our international operations, increase our operating costs and hinder our ability to grow our international business and, consequently, our overall business and results of operations. In addition, if the political and military situation in Russia and the Ukraine, or the relationship between Russia and the United States, significantly worsens, or if either Russia or the United States imposes significant new economic sanctions or restrictions on doing business, and we are restricted or precluded from continuing our software development

Table of Contents

operations in Russia, our costs could increase, and our product development efforts, business and results of operations could be significantly harmed.

In addition, compliance with laws and regulations applicable to our international operations increases our cost of doing business outside the United States. We may be unable to keep current with changes in foreign government requirements and laws as they change from time to time. Failure to comply with these regulations could harm our business. In many countries outside the United States it is common for others to engage in business practices that are prohibited by our internal policies and procedures or U.S. or international regulations applicable to us. Although we have implemented policies and procedures designed to ensure compliance with these laws and policies, there can be no assurance that all of our employees, contractors, strategic partners and agents will comply with these laws and policies. Violations of laws or key control policies by our employees, contractors, strategic partners or agents could result in delays in revenue recognition, financial reporting misstatements, fines, penalties, or prohibitions on selling our solution, any of which could harm our business.

We have undergone recent changes to our management team; we depend on our senior management team, and the loss of one or more key employees or an inability to attract and retain highly skilled executives and other employees could harm our business and results of operations.

Our former Chief Executive Officer resigned for health reasons (though he remains as Executive Chairman of our Board of Directors) effective December 2, 2017, resulting in the appointment of our Chief Financial Officer as Interim Chief Executive Officer, the promotion of our EVP of Global Sales and Services to President, and the commencement of a search for a new Chief Executive Officer. On May 1, 2018, we announced the appointment, effective as of May 3, 2018, of a new Chief Executive Officer. In connection with this appointment, our Chief Financial Officer will no longer serve as Interim Chief Executive Officer, but will continue to serve as our Chief Financial Officer.

Our success depends, in part, upon the performance and continued services of our key executive officers. If our new executive leadership team fails to perform effectively or if we fail to retain these executives or other members of our executive leadership team, our business, financial condition or results of operations could be harmed. We also rely on our leadership team in the areas of research and development, marketing, sales, services and general and administrative functions, and on mission-critical individual contributors. The loss of one or more of our executive officers or key employees could seriously harm our business. We currently do not maintain key person life insurance policies on any of our employees.

To execute our growth plan, we must attract and retain highly qualified personnel and we may incur significant costs to do so. Competition for these personnel is intense, especially for senior executives, engineers highly experienced in designing and developing cloud software and for senior sales personnel. We have, from time to time, experienced, and we expect to continue to experience, difficulty in hiring and retaining employees with appropriate qualifications. We invest significant time and expense in training our employees, which increases their value to competitors who may seek to recruit them and increases our costs. If we fail to attract new personnel or fail to retain and motivate our current personnel, particularly our senior executives, our business and future growth prospects would be harmed. Many of the companies with which we compete for experienced personnel have greater resources than we have. If we hire employees from competitors or other companies, their former employers may attempt to assert that these employees or we have breached legal obligations, resulting in a diversion of our time and resources and, potentially, damages.

Volatility or lack of performance in the trading price of our common stock may also affect our ability to attract and retain qualified personnel because job candidates and existing employees often emphasize the value of the stock awards they receive in connection with their employment when considering whether to accept or continue employment. If the perceived value of our stock awards is low or declines, it may harm our ability to recruit and retain highly skilled employees.

If we fail to grow our marketing capabilities and develop widespread brand awareness cost effectively, our business may suffer.

Our ability to increase our client base and achieve broader market acceptance of our cloud contact center software solution will depend to a significant extent on our ability to expand our marketing operations. We plan to continue to dedicate significant resources to our marketing programs, including internet advertising, digital marketing campaigns, social marketing, trade shows, industry events, co-marketing with strategic partners and

Table of Contents

telemarketing. The effectiveness of our online advertising has varied over time and may vary in the future due to competition for key search terms, changes in search engine use and changes in the search algorithms used by major search engines. All of these efforts will continue to require us to invest significant financial and other resources in our marketing efforts. Our business will be seriously harmed if our efforts and expenditures do not generate a proportionate increase in revenue.

In addition, we believe that developing and maintaining widespread awareness of our brand in a cost-effective manner, both in the United States and internationally, is critical to achieving widespread acceptance of our solution and attracting new clients. Brand promotion activities may not generate client awareness or increase revenues, and even if they do, any increase in revenues may occur after the expense has been occurred, and may not offset the costs and expenses of building our brand. If we fail to successfully promote, maintain and protect our brand, or incur substantial costs and expenses, we may fail to attract or retain clients necessary to realize a sufficient return on our brand-building efforts, or to achieve the widespread brand awareness that is critical for broad client adoption of our solution.

We may not be able to secure additional financing on favorable terms, or at all, to meet our future capital needs.

To date, we have financed our operations, primarily through sales of our solution, lease facilities and the net proceeds from our equity and debt financings. We do not know when or if our operations will generate sufficient cash to fund our ongoing operations. We may require additional capital to respond to business opportunities, challenges, acquisitions, a decline in sales, increased regulatory obligations or unforeseen circumstances and may engage in equity or debt financings or enter into credit facilities.

We have a substantial amount of debt. As of March 31, 2018, we had approximately $32.6 million in principal amount outstanding under our Revolving Credit Facility entered into on August 1, 2016 and a $0.2 million FCC civil penalty payable to the U.S. Treasury. See Note 6 of the notes to condensed consolidated financial statements.

Our Revolving Credit Facility is collateralized by substantially all of our assets and contains a number of covenants that limit our ability to, among other things, sell assets, make acquisitions or investments, incur debt, grant liens, pay dividends, enter into transactions with our affiliates and use all of our available cash on hand and may prevent us from engaging in acts that may be in our best long-term interests. The amount of our current total debt and the collateral pledged under the Revolving Credit Facility and the covenants to which we are bound may prevent us from being able to timely secure additional debt or equity financing on favorable terms, or at all, or to pursue business opportunities, including potential acquisitions. Any debt financing obtained by us in the future would cause us to incur additional debt service expenses and could include additional restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and pursue business opportunities. If we raise additional funds through further issuances of equity or convertible debt securities, our existing stockholders could suffer significant dilution in their percentage ownership of our company, and any new equity securities we issue could have rights, preferences and privileges senior to those of holders of our common stock. If we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to grow and support our business and to respond to business challenges could be significantly limited.

Adverse economic conditions may harm our business.

Our business depends on the overall demand for cloud contact center software solutions and on the economic health of our current and prospective clients. In addition to the United States, Canada and Latin America, we plan to market and sell our solution in Europe, Asia and other international markets. If economic conditions, including currency exchange rates, in these areas and other key potential markets for our solution continue to remain uncertain or deteriorate, clients may delay or reduce their contact center and overall information technology spending. If our clients experience economic hardship, this could reduce the demand for our solution, delay and lengthen sales cycles, lower prices for our solution, and lead to slower growth or even a decline in our revenues, operating results and cash flows.

We may acquire other companies or technologies or be the target of strategic transactions, which could divert our management’s attention, result in additional dilution to our stockholders and otherwise disrupt our operations and harm our operating results.

We may acquire or invest in businesses, applications or technologies that we believe could complement or expand our solution, enhance our technical capabilities or otherwise offer growth opportunities. The pursuit of

Table of Contents

potential acquisitions may divert the attention of management, and cause us to incur various costs and expenses in identifying, investigating and pursuing acquisitions, whether or not they are consummated. We may not be able to identify desirable acquisition targets or be successful in entering into an agreement with any particular target.

To date, the growth in our business has been primarily organic, and we have limited experience in acquiring other businesses, having only completed one small acquisition in 2013. In any future acquisitions, we may not be able to successfully integrate acquired personnel, operations and technologies, or effectively manage the combined business following the acquisition. We also may not achieve the anticipated benefits from our future acquired businesses due to a number of factors, including:

- inability to integrate or benefit from acquisitions in a profitable manner;
- unanticipated costs or liabilities associated with the acquisition, including legal claims arising from the activities of companies we acquire;
- acquisition-related costs;
- difficulty converting the clients of the acquired business to our solution and contract terms, including due to disparities in the revenue, licensing, support or professional services model of the acquired company;
- difficulty integrating the accounting systems, operations and personnel of the acquired business;
- difficulties and additional costs and expenses associated with supporting legacy products and the hosting infrastructure of the acquired business;
- diversion of management’s attention from other business concerns;
- harm to our existing relationships with our partners and clients as a result of the acquisition;
- the loss of our or the acquired business’s key employees;
- diversion of resources that could have been more effectively deployed in other parts of our business; and
- use of substantial portions of our available cash to consummate the acquisition.

In addition, a significant portion of the purchase price of companies we acquire may be allocated to acquired goodwill and other intangible assets, which must be assessed for impairment at least annually. In the future, if our acquisitions do not yield expected returns, we may be required to take charges to our operating results based on this impairment assessment process, which could harm our results of operations.

Acquisitions could also result in dilutive issuances of equity securities, the use of our available cash, or the incurrence of debt, which could harm our operating results. In addition, if an acquired business fails to meet our expectations, our operating results, business and financial condition may suffer.

In addition, third parties may be interested in acquiring us. We will continue to consider and discuss such transactions as we deem appropriate. Such potential transactions may divert the attention of management, and cause us to incur various costs and expenses in investigating and evaluating such transactions, whether or not they are consummated.

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

As a public company, we are required to maintain internal control over financial reporting and to report any material weaknesses in such internal controls. Section 404 of the Sarbanes-Oxley Act of 2002, or Section 404, requires that we evaluate and determine the effectiveness of our internal control over financial reporting and provide a management report on our internal control over financial reporting. Beginning with our annual report for the year ended December 31, 2017, our independent registered public accounting firm was required to provide this attestation, which has and will continue to increase our cost and expense.

If we identify one or more material weaknesses in our internal control over financial reporting, we will be unable to assert that our internal controls are effective. A “material weakness” is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

If we have material weaknesses in our internal control over financial reporting, we may not detect errors on a timely basis and our financial statements may be materially misstated. If we identify material weaknesses in our internal control over financial reporting, if we are unable to comply with the requirements of Section 404 in a timely

Table of Contents

manner, if we are unable to assert that our internal control over financial reporting is effective or if our independent registered public accounting firm is unable to attest that our internal control over financial reporting is effective, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock could decrease. We could also become subject to stockholder or other third-party litigation as well as investigations by the stock exchange on which our securities are listed, the SEC or other regulatory authorities, which could require additional financial and management resources and could result in fines, trading suspensions or other remedies.

We are no longer an emerging growth company and the additional requirements we must comply with may strain our resources and divert management’s attention from other business concerns.

We are no longer an “emerging growth company” as defined in the JOBS Act. While we were an emerging growth company, we were able to take advantage of certain exemptions from reporting requirements that are applicable to other public companies. Compliance with these additional laws, rules and regulations has and will continue to increase our legal and financial compliance costs, make some activities more difficult, time consuming or costly and increase demand on our systems and resources. As a result, management’s attention may be diverted from other business concerns and our costs and expenses will increase, which could harm our business and operating results. We may also need to hire more employees in the future or engage additional outside consultants to comply with these requirements, which will increase our costs and expenses.

Changes in financial accounting standards or practices may cause adverse, unexpected financial reporting fluctuations and affect our reported operating results.

U.S. GAAP is subject to interpretation by the FASB, the SEC and various bodies formed to promulgate and interpret appropriate accounting principles. A change in accounting standards or practices can have a significant effect on our reported results and may even affect our financial statements completed before the change is effective. New accounting pronouncements and varying interpretations of accounting pronouncements have occurred and will occur in the future. Changes to existing rules or the questioning of current practices may harm our reported financial results or the way we account for or conduct our business.

For example, in May 2014, the FASB issued new revenue recognition rules under Accounting Standard Codification 606 - Revenue from Contracts with Customers (“ASC 606”), which included a single set of rules and criteria for revenue recognition to be used across all industries. We adopted this new standard in January 2018 using a modified retrospective method. With the adoption of this standard, the timing of our commission expense recognition changed, which caused fluctuations in our operating results. See Note 2 of the notes to condensed consolidated financial statements for information regarding the effect of new accounting pronouncements on our financial statements. The application of new accounting guidance including ASC 606 will be based on all information available to us as of the date of adoption and up through subsequent interim reporting, including transition guidance published by the standard setters. However, the interpretation of these new standards will continue to evolve as other public companies adopt the new guidance and the standard setters issue new interpretative guidance related to these rules. As a result, changes in the interpretation of these rules could result in material adjustments to our application of the new guidance, which could have a material effect on our results of operations and financial condition. Additionally, any difficulties in implementing these pronouncements could cause us to fail to meet our financial reporting obligations, which could result in regulatory discipline and harm investors’ confidence in us.

In addition, certain factors have in the past and may in the future cause us to defer recognition of revenues. For example, the inclusion in our client contracts of material non-standard terms, such as acceptance criteria, could require the deferral of revenue. To the extent that such contracts become more prevalent in the future our revenue may be harmed.

Because of these factors and other specific requirements under U.S. GAAP for revenue recognition, we must have precise terms and conditions in our arrangements in order to recognize revenue when we deliver our solution or perform our professional services. Negotiation of mutually acceptable terms and conditions can extend our sales cycle, and we may accept terms and conditions that do not permit revenue recognition at the time of delivery.

Table of Contents

The results of the United Kingdom's referendum on withdrawal from the European Union may have a negative effect on global economic conditions, financial markets and our business.

In June 2016, a majority of voters in the United Kingdom elected to withdraw from the European Union in a national referendum, referred to as Brexit. The referendum was advisory, and the terms of any withdrawal are subject to a negotiation period that could last at least two years after the government of the United Kingdom formally initiated the withdrawal process on March 29, 2017. This election to withdraw has created significant uncertainty about the future relationship between the United Kingdom and the European Union, including with respect to the laws and regulations that will apply as the United Kingdom and the European Union determine which European Union laws to replace or replicate after the effectiveness of the withdrawal. The referendum has also given rise to calls for the governments of other European Union member states to consider withdrawal.

Brexit has harmed and may continue to harm global economic conditions and the stability of global financial markets. For example, Brexit introduced significant volatility in global stock markets and currency exchange rate fluctuations that resulted in the strengthening of the U.S. dollar against foreign currencies in which we conduct business. This volatility will likely continue while the United Kingdom and the European Union negotiate the terms of the withdrawal, as well as after the withdrawal takes effect. The strengthening of the U.S. dollar relative to other currencies will make our solution more expensive to international clients and may harm our international sales. Brexit could also cause disruptions to and create uncertainty surrounding our business, including affecting our relationships with our existing and future clients, owners of our data center facilities in the U.K. and the Netherlands and our data center partners' ability to retain and hire qualified employees, which could harm our business, business opportunities, results of operations, financial condition and cash flows.

We may not be able to utilize a significant portion of our net operating loss or research tax credit carryforwards, and under recently enacted lower federal corporate tax rates such tax benefits will be of less value, which could harm our profitability and financial condition.

As of December 31, 2017, we had federal and state net operating loss carryforwards due to prior period losses of $188.8 million and $104.4 million, respectively, which if not utilized will begin to expire in 2024 for federal purposes. The state net operating loss started to expire in 2017. As of December 31, 2017, we also had research credit carryforwards for federal and California state tax purposes of $2.8 million and $2.4 million. If not utilized, the federal research credit carryforwards will begin to expire in 2022. If we are unable to generate sufficient taxable income to utilize our net operating loss and research tax credit carryforwards, these carryforwards could expire unused and be unavailable to offset future income tax liabilities, which could harm our profitability and financial condition.

In addition, under Section 382 of the Internal Revenue Code of 1986, as amended, or IRC Section 382, our ability to utilize net operating loss carryforwards or other tax attributes, such as research tax credits, in any taxable year may be limited if we experience an "ownership change." An IRC Section 382 "ownership change" generally occurs if one or more stockholders or groups of stockholders who own at least 5% of our stock increase their ownership by more than 50 percentage points over their lowest ownership percentage within a rolling three-year period. Similar rules may apply under state tax laws. We experienced an ownership change prior to 2014 and the disclosed amounts of our net operating losses and potential tax credits have been reduced for the resulting effect of the IRC Section 382 limitations. Subsequent or future issuances or sales of our stock (including certain transactions involving our stock that are outside of our control) could cause an "ownership change" again, which would impose an annual limit on the amount of pre-ownership change net operating loss carryforwards and other tax attributes we can use to reduce our taxable income, potentially increasing and accelerating our liability for income taxes, and also potentially causing those tax attributes to expire unused. It is possible that such an ownership change could materially reduce our ability to use our net operating loss carryforwards or other tax attributes to offset taxable income, which could require us to pay more income taxes than if we were able to fully utilize our net operating loss carryforwards and harm our profitability.

We continue to assess the impact of recently enacted H.R. 1, commonly referred to as the Tax Cuts and Jobs Act, or the new tax law, as well as any future regulations implementing the new tax law and any interpretations of the new tax law. The effect of those regulations and interpretations, as well as any additional tax reform legislation in the United States or elsewhere, could harm our business and financial condition by, among other things, decreasing the value of our net operating loss carryforwards. If we are required to reduce the value of our net operating loss carryforwards, we may be required to record a corresponding charge to current earnings, which could harm our financial condition and results of operations in the period in which it is recorded.

Table of Contents

Risks Related to Our Intellectual Property

Any failure to protect our intellectual property rights could impair our ability to protect our proprietary technology and our brand.

Our success and ability to compete depend in part upon our intellectual property. As of March 31, 2018, our intellectual property portfolio included seven registered U.S. trademarks, 10 issued U.S. patents, two pending U.S. patent applications and one registered U.S. copyright. As of March 31, 2018, we also had two issued patents, two pending patent applications and 11 trademark registrations outside the U.S. The expiration dates of our issued patents range from 2030 to 2034. We primarily rely on copyright, trade secret and trademark laws, trade secret protection and confidentiality or license agreements with our employees, clients, partners and others to protect our intellectual property rights. However, the steps we take to secure, protect and enforce our intellectual property rights may be inadequate. We may not be able to obtain any further patents or trademarks, our current patents could be invalidated or our competitors could design their products around our patented technology, and our pending applications may not result in the issuance of patents or trademarks. We have pending patent applications and trademark registrations outside the U.S., and we may have to expend significant additional resources to obtain additional protection and maintain current registrations as we expand our international operations. Furthermore, legal standards relating to the validity, enforceability and scope of protection of intellectual property rights in other countries, including Russia, where we have significant research and development operations, and the Philippines, where we have significant technical support, training and other professional services are performed, are uncertain and may afford little or no effective protection of our proprietary technology, and the risk of intellectual property misappropriation may be higher in these countries. Consequently, we may be unable to prevent our proprietary technology from being exploited abroad, which could affect our ability to expand into international markets or require costly efforts to protect our technology.

In order to protect our intellectual property rights, we may be required to spend significant resources to monitor and protect these rights. Litigation brought to protect and enforce our intellectual property rights could be costly, time consuming and distracting to management and could result in the impairment or loss of our intellectual property. Furthermore, our efforts to enforce our intellectual property rights may be met with defenses, counterclaims and countersuits attacking the validity and enforceability of our intellectual property rights. Accordingly, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property. Our failure to secure, protect and enforce our intellectual property rights could substantially harm the value of our technology, solutions, brand and business.

We will likely continue to be subject to third-party intellectual property infringement claims.

There is considerable patent and other intellectual property development activity and litigation in our industry. Our success depends upon our not infringing upon the intellectual property rights of others. Our competitors, as well as a number of other entities and individuals, may own or claim to own intellectual property relating to our industry. From time to time, third parties have claimed that we are infringing upon their intellectual property rights. For example, NobelBiz, Inc., or NobelBiz, filed a patent infringement lawsuit against us alleging that our local caller ID management service infringed on certain of its patents. In December 2017, the lawsuit was settled and the case was dismissed in its entirety.

Certain technology necessary for us to provide our solution may be patented, copyrighted or otherwise protected by other parties either now or in the future. In such case, we would have to negotiate a license for the use of that technology. We may not be able to negotiate such a license at a price that is acceptable, or at all. The existence of such a patent, copyright or other protections, or our inability to negotiate a license for any such technology on acceptable terms, could force us to cease using such technology and offering solutions incorporating such technology.

Others have claimed, or in the future may claim, that our solution and underlying technology infringe or violate their intellectual property rights. However, we may be unaware of the intellectual property rights that others may claim cover some or all of our technology or solution. Any claims or litigation could cause us to incur significant costs and expenses and, if successfully asserted against us, could require that we pay substantial damages or ongoing royalty payments, require that we refrain from using, manufacturing or selling certain offerings or features or using certain processes, prevent us from offering our solution or certain features thereof, or require that we comply with other unfavorable terms, any of which could harm our business and operating results. We may also be obligated to indemnify our clients or business partners or pay substantial settlement costs, including royalty payments, in connection with any such claim or litigation and to obtain licenses, modify applications, or refund fees,

Table of Contents

which could be costly. Even if we were to prevail in such a dispute, any litigation regarding our intellectual property could be costly and time consuming and divert the attention of our management and key personnel from our business operations.

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

Our solution incorporates certain third-party software obtained under licenses from other companies. We anticipate that we will continue to rely on such software and development tools from third parties in the future. Although we believe that there are commercially reasonable alternatives to the third-party software we currently license, this may not be the case, or it may be difficult or costly to transition to other providers. In addition, integration of the software used in our solution with new third-party software may require significant work and require substantial investment of our time and resources. To the extent that our solution depends upon the successful operation of third-party software in conjunction with our software, any undetected errors or defects in this third-party software could prevent the deployment or impair the functionality of our solution, delay new product or solution introductions, result in increased costs, or a failure of our solution and injure our reputation. Our use of additional or alternative third-party software would require us to enter into license agreements with third parties and to integrate such software to our solution. There can be no assurance that the technology licensed by us will continue to provide competitive features and functionality or that licenses for technology currently utilized by us or other technology that we may seek to license in the future, will be available to us at a reasonable cost or on commercially reasonable terms, or at all. Third-party licensors may also be acquired or go out of business, which could preclude us from continuing to use such technology. The loss of, or inability to maintain, existing licenses could result in lost product features and litigation. The loss in existing licenses could also result in implementation delays or reductions until equivalent technology or suitable alternative solutions could be developed, identified, licensed and integrated, and could increase our costs and harm our business.

Our solution utilizes open source software, and any failure to comply with the terms of one or more of these open source licenses could negatively affect our business.

Our solution includes software covered by open source licenses, which may include, for example, free general public use licenses, open source front-end libraries and open source applications. The terms of various open source licenses have not been interpreted by United States courts, and there is a risk that such licenses could be construed in a manner that imposes unanticipated conditions or restrictions on our ability to market our solution. By the terms of certain open source licenses, we could be required to release the source code of our proprietary software, and to make our proprietary software available under open source licenses, if we combine our proprietary software with open source software in a certain manner. In the event that portions of our proprietary software are determined to be subject to an open source license, we could be required to publicly release the affected portions of our source code, re-engineer all or a portion of our technologies, or otherwise be limited in the licensing of our technologies, each of which could reduce or eliminate the value of our technologies and solutions. In addition to risks related to license requirements, usage of open source software can lead to greater risks than use of third-party commercial software, as open source licensors generally do not provide warranties or controls on the origin of the software. Given the nature of open source software, there is also a risk that third parties may assert copyright and other intellectual property infringement claims against us based on our use of certain open source software programs. Many of the risks associated with the usage of open source software cannot be eliminated, and could harm our business.

Risks Related to Regulatory Matters

Failure to comply with laws and regulations could harm our business and our reputation.

Our business is subject to regulation by various federal, state, local and foreign governmental agencies, including agencies responsible for monitoring and enforcing employment and labor laws, workplace safety, environmental laws, consumer protection laws, anti-bribery laws, import/export controls, federal securities laws and tax laws and regulations. In certain jurisdictions, these regulatory requirements may be more stringent than those in the United States and in other circumstances these requirements may be more stringent in the United States. Noncompliance with applicable regulations or requirements could subject us to investigations, sanctions, mandatory recalls, enforcement actions, disgorgement of profits, fines, damages, civil and criminal penalties or injunctions. If any governmental sanctions, fines or penalties are imposed, or if we do not prevail in any possible civil or criminal litigation, our business, operating results, financial condition and our reputation could be harmed. In addition, responding to any action will likely result in a significant diversion of management's attention and resources and an increase in professional fees. Enforcement actions and sanctions could further harm our business, operating results, financial condition and our reputation.

Alleged or actual failure to comply with the constantly evolving legal and contractual environment surrounding calling consumers and wireless phone numbers by other companies or our competitors or governmental or private enforcement actions related thereto, could harm our business, financial condition, results of operations and cash flows.

The legal and contractual environment surrounding calling consumers and wireless phone numbers is constantly evolving. In the United States, two federal agencies, the Federal Trade Commission, or FTC and the FCC, and various states have laws including, at the federal level, the Telephone Consumer Protection Act of 1991, or TCPA, that restrict the placing of certain telephone calls and texts to residential and wireless telephone subscribers by means of automatic telephone dialing systems, prerecorded or artificial voice messages and fax machines. These laws require companies to institute processes and safeguards to comply with these restrictions. Some of these laws, where a violation is established, can be enforced by the FTC, FCC, State Attorneys General, or private party litigants. In these types of actions, the plaintiff may seek damages, statutory penalties, costs and/or attorneys' fees.

We have designed our solution to comply with these laws. To the extent that our solution is viewed by clients or potential clients as less functional, or more difficult to deploy or use, because of our solution's compliance features, we may lose market share to competitors that do not include similar compliance safeguards. Our contractual arrangements with our clients who use our solution to place calls also expressly require them to comply with all such laws and to indemnify us for any failure to do so. We take reasonable steps to confirm such compliance. Even with these efforts, it is possible that the FTC, FCC, private litigants or others may attempt to hold our clients, or us as a software provider, responsible for alleged violations of these laws. It also is possible that we may not successfully enforce or collect upon our contractual indemnities from our clients. Additionally, these laws, and any changes to them or the interpretation thereof, that further restrict calling consumers, including to wireless phone numbers, adverse publicity regarding the alleged or actual failure by companies, including our clients and competitors, to comply with such laws or governmental or private enforcement actions related thereto, could result in a reduction in the use of our solution by our clients and potential clients, which could harm our business, financial condition, results of operations and cash flows.

Increased taxes on our service may increase our clients' cost of using our service and/or increase our costs and reduce our profit margins to the extent the costs are not passed through to our clients, and we may be subject to liabilities for past sales and other taxes, surcharges and fees.

During 2011, we analyzed our activities and determined that we were obligated to collect sales taxes on sales of our subscription services in certain U.S. states. Accordingly, we registered with those states and, in 2012, commenced paying past-due amounts and collecting sales taxes from our clients and remitting such taxes to the applicable state taxing authorities. Prior to 2012, we did not collect or remit U.S. state or local sales, use, gross receipts, excise and utility user taxes, fees or surcharges on our solution. During the first quarter of 2015, we conducted an updated review of the taxability of sales of our subscription services and identified four additional U.S. states where we may be obligated to collect and remit sales taxes.

During 2013, we analyzed our activities and determined that we may be obligated to collect and remit sales, excise and utility user taxes, as well as surcharges as a communications service provider, and pay gross receipts taxes, on our usage-based fees in certain U.S. states and municipalities. We neither collected nor remitted state and local taxes or surcharges on usage-based fees in any of the periods prior to 2014. Based on our ongoing assessment of our U.S. state and local tax collection and remittance obligations in respect of usage-based fees, in 2014, we registered for tax and regulatory purposes in all U.S. states where we determined such registration is proper and commenced collecting and remitting applicable state and local taxes and surcharges on such fees.

We have accrued a contingent liability of $1.4 million for our best estimate of the probable amount of taxes and surcharges that may be imposed by various states and municipalities on our activities, including our usage-based and subscription services, prior to registration. This contingent liability is based on our analysis of a number of factors, including the source location of our usage-based fees, the taxability of our subscription services and the rules and regulations in each state. The actual amount of state and local taxes and surcharges paid may differ from our estimates. See Note 10 of the notes to condensed consolidated financial statements.

While we have accrued for these potential liabilities in each period, such accruals are based on analyses of our business activities, the operation of our solution, applicable statutes, regulations and rules in each state and locality and estimates of sales subject to sales tax or other charges. State and local taxing and regulatory authorities may challenge our position and may decide to audit our business and operations with respect to state or local sales, use, gross receipts, excise and utility user taxes, fees or surcharges, which could result in our being liable for taxes, fees, or surcharges, as well as related penalties and interest, above our recorded accrued liability or additional liability for taxes, fees, or surcharges, as well as penalties and interest for our clients, which could harm our results of operations and our relationships with our clients. In addition, if our international sales grow, additional foreign countries may seek to impose sales or other tax collection obligations on us, which would increase our exposure to liability.

The applicability of state or local taxes, fees or surcharges relative to services such as ours is complex, ambiguous and subject to interpretation and change. If states enact new legislation or if taxing and regulatory authorities promulgate new rules or regulations or expand or otherwise alter their interpretations of existing rules and regulations, we could incur additional liabilities. In addition, the collection of additional taxes, fees or surcharges in the future could increase our prices or reduce our profit margins. Compliance with new or existing legislation, rules or regulations may also make us less competitive with those competitors who are not subject to, or choose not to comply with, such legislation, rules or regulations. We have incurred, and will continue to incur, substantial ongoing costs associated with complying with state or local tax, fee or surcharge requirements in the numerous markets in which we conduct or will conduct business.

Our ability to offer services outside the U.S. is subject to different regulatory and taxation requirements, which may be complicated and uncertain.

As we continue to expand the sale and implementation of our solutions internationally, we will be subject to new regulations, taxes, surcharges and fees. Compliance with these new complex regulatory requirements that differ from country to country and are frequently changing may impose substantial compliance burdens on our business. At times, it may be difficult to determine which laws and regulations apply, we may discover that we are required to comply with certain laws and regulations after having provided services for some time in that jurisdiction, which could subject us to retroactive taxes, fees and penalties, and we may be subject to conflicting requirements. For example, prior to 2016, we had not collected taxes on our sales in Canada. During the second quarter of 2015, we reviewed the taxability of our sales in Canada and determined that we were obligated to collect from our Canadian clients and remit to the Canadian federal and certain provincial governments Value-added Taxes, or VAT, and/or Provincial Sales Taxes, or PST. We commenced collecting and remitting such taxes in January 2016. Additionally, as we expand internationally, the risk that governments will regulate or impose new or increased taxes or fees on our services increases. Any such additional regulation or taxes could decrease the value of our international expansion and harm our results of operations.

We are subject to assessments for unpaid USF contributions, as well as interest thereon and civil penalties, due to our late registration and past failure to recognize our obligation as a USF contributor and as an international carrier.

During the third quarter of 2012, we determined that based on our business activities, we are classified as a telecommunications service provider for regulatory purposes and we are required to make direct contributions to the USF based on revenue we receive from the resale of interstate and international telecommunications services. In order to comply with the obligation to make direct contributions, in November 2012, we made a voluntary self-disclosure to the FCC Enforcement Bureau and have registered with the USAC which is charged by the FCC with administering the USF. In April 2013, we began remitting required contributions on a prospective basis directly to USAC.

Our registration with USAC subjects us to assessments for unpaid USF contributions, as well as interest thereon and civil penalties, due to our late registration and past failure to recognize our obligation as a USF contributor and as an international carrier. We are required to pay assessments for periods prior to our registration. As of December 31, 2012, our total past due USF contribution being imposed by USAC and accrued by us for the period from 2003 through 2012 was $8.1 million, of which $4.7 million was undisputed and $3.4 million was disputed. We subsequently updated our filings and increased the liability related to 2008 through 2012 by $0.5 million, arriving at a new total of $3.9 million in disputed liability. As of January 31, 2017, we had fully paid the promissory note issued to USAC for the undisputed portion. In January 2017, the FCC ruled in our favor with respect to most of the disputed amount. In September 2017, USAC issued a credit to us reflecting the FCC's ruling for the $3.1 million of the $3.9 million in disputed liability. In addition, USAC reversed the interest and penalties related to the disputed liability of $3.1 million. The remaining $0.8 million in dispute involves USAC's assessment of liability for the period of 2003 through 2007, which was prior to the five year window during which we were required to maintain financial records for USF contribution purposes. In 2013, we filed a Request for Review (a form of appeal) of this disputed amount with the FCC, which remains pending. If the Request for Review is not resolved in our favor, it is possible that we will be held to the back assessments of $0.8 million, which includes interest and penalties on that amount.

In 2012, we also determined that we were a provider of international telecommunications services and therefore we were required to secure from the FCC a section 214 international carrier authorization permitting such international telecommunications. We applied with the FCC for international carrier authority, which was granted on June 9, 2015. On June 12, 2015, in connection with our late registration with the USAC and past failure to recognize our obligation as a USF contributor and as an international carrier from 2003 to 2012, we entered into a consent decree with the FCC Enforcement Bureau. In the consent decree, we agreed to pay a civil penalty of $2.0 million to the U.S. Treasury in twelve equal quarterly installments starting in July 2015 without interest. In the third quarter of 2014, we had accrued a $2.0 million liability for the then tentative civil penalty, of which $0.2 million in principal remained outstanding as of March 31, 2018. The consent decree also requires us to adopt certain internal regulatory compliance monitoring and training requirements, and to report on the status of those compliance efforts to the FCC's Enforcement Bureau during a period of three years. Our implementation of the internal regulatory compliance monitoring and training requirements were completed in August 2015, and the annual compliance reporting to the FCC will continue until June 2018. To the extent that we do not comply with these obligations, we could be subject to further enforcement action, including fines and penalties, by the FCC. See Note 10 of the notes to condensed consolidated financial statements.

Our ongoing obligations to pay federal, state and local telecommunications contributions and taxes may decrease our price advantage over our competitors who have historically paid these contributions and taxes and could also make us less competitive with those competitors who are not subject to, or choose not to comply with, those requirements. In addition, if we are unable to continue to pass some or all of the cost of these contributions and taxes to our clients, our profit margins on the minutes we resell will decrease. Our federal contributions and tax obligations may significantly increase in the future, due to new interpretations by governing authorities, governmental budget pressures, changes in our business model or solutions or other factors.

If we do not comply with FCC rules and regulations, we could be subject to further FCC enforcement actions, fines, loss of licenses and possibly restrictions on our ability to operate or offer certain of our services.

Since our business is regulated by the FCC, we are subject to existing or potential FCC regulations relating to privacy, disability access, porting of numbers, USF contributions and other requirements. If we do not comply with FCC rules and regulations, we could be subject to further FCC enforcement actions, fines, loss of licenses and possibly restrictions on our ability to operate or offer certain of our services. Any further enforcement action by the FCC, which may be a public process, would hurt our reputation in the industry, possibly impair our ability to sell our services to clients and could harm our business and results of operations.

The regulations to which we are subject (in whole or in part) include:

- the Communications Assistance for Law Enforcement Act, or CALEA, which requires covered entities to assist law enforcement in undertaking electronic surveillance;
- contributions to the USF which requires that we pay a percentage of our revenues resulting from the provision of interstate telecommunications services to support certain federal programs;
- payment of annual FCC regulatory fees based on our interstate and international revenues;
- rules pertaining to access to our services by people with disabilities and contributions to the Telecommunications Relay Services fund; and
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FCC rules regarding Customer Proprietary Network Information, or CPNI, which prohibit us from using such information without client approval, subject to certain exceptions.

Table of Contents

If we do not comply with any current or future rules or regulations that apply to our business, we could be subject to additional and substantial fines and penalties, we may have to restructure our service offerings, exit certain markets, accept lower margins or raise the price of our services, any of which could harm our business and results of operations.

Reform of federal and state USF programs could increase the cost of our service to our clients, diminishing or eliminating our pricing advantage.

The FCC and a number of states are considering reform or other modifications to USF programs. The way we calculate our contribution may change if the FCC or certain states engage in reform or adopt other modifications. In April 2012, the FCC released a Further Notice of Proposed Rulemaking to consider reforms to the manner in which companies like us contribute to the federal USF program. In general, the Further Notice of Proposed Rulemaking is considering questions like: what companies should contribute, how contributions should be assessed, and methods to improve the administration of the system. We cannot predict the outcome of this proceeding nor its impact on our business at this time. The changes in the leadership of the U.S. Government resulting from the federal election in 2016 may renew interest in completing this proceeding.

Should the FCC or certain states adopt new contribution mechanisms or otherwise modify contribution obligations that increase our contribution burden, we will either need to raise the amount we currently collect from our clients to cover this obligation or absorb the costs, which would reduce our profit margins. Furthermore, the FCC has ruled that states can require us to contribute to state USF programs. A number of states already require us to contribute, while others are actively considering extending their programs to include the solution we provide. Currently our USF contributions are borne by our clients, which could result in our solution becoming less competitive as compared to products provided by our competitors.

Privacy concerns and domestic or foreign laws and regulations may reduce the demand for our solution, increase our costs and harm our business.

Our clients can use our solution to collect, use and store information, including personally identifiable information or other information treated as confidential, regarding their customers and potential customers. Federal, state and foreign government bodies and agencies have adopted, are considering adopting, or may adopt laws and regulations regarding the collection, use, storage and disclosure of such information obtained from consumers and individuals. The costs of compliance with, and other burdens imposed by, such laws and regulations that are applicable to us and the businesses of our clients may limit the use and adoption of our solution and reduce overall demand, or lead to significant fines, penalties or other regulatory liabilities such as orders or consent decrees forcing us to modify our business practices, as well as reputational damage or third-party lawsuits for any noncompliance with such laws. Furthermore, privacy and data protection concerns may cause consumers to resist providing the personal data necessary to allow our clients to use our solution effectively. Even the perception of privacy concerns, whether or not valid, may inhibit market adoption of our solution in certain industries or countries.

Domestic and international legislative and regulatory initiatives may harm our clients' ability to process, handle, store, use and transmit information, including demographic and personally identifiable information or other information treated as confidential, regarding their customers, which could reduce demand for our solution. These laws and regulations are still evolving and are likely to be in flux and subject to uncertain interpretation for the foreseeable future. Our business could be harmed if legislation or regulations are adopted, interpreted or implemented in a manner that is inconsistent from country to country and inconsistent with our current policies and practices, or those of our clients. In addition, foreign data protection, privacy, and consumer protection laws and regulations are often more stringent than those in the United States. In particular, the European Union and its member states traditionally have imposed greater legal obligations on companies that collect and process personal data.

In October 2015, the Court of Justice for the European Union invalidated the U.S.-EU Safe Harbor program, or the Safe Harbor. The Safe Harbor provided participating U.S. companies with a legal basis to comply with EU data transfer regulations that would otherwise restrict the transfer of personal data by our clients from the European Union to us in the United States. Some of our clients relied on the Safe Harbor to transfer the personal data of their customers located in the EU to the United States. Other clients relied on legally recognized alternative mechanisms such as standard contractual clauses issued by the European Commission (commonly referred to as “model contracts”) or binding corporate resolutions to make such transfers. We relied on the use of standard contractual clauses issued by the European Commission before the invalidation of the Safe Harbor in October 2015, and we

Table of Contents

continue to do so currently. In July 2016, EU and U.S. regulators announced the approval of a new trans-Atlantic Agreement, the EU-U.S. Privacy Shield, or the Privacy Shield, which succeeds the Safe Harbor. Companies interested in self-certifying compliance with this new trans-Atlantic data-transfer framework could do so beginning in August 2016, when the U.S. Department of Commerce began accepting certifications. The self-certification process under the Privacy Shield is similar to the Safe Harbor. However, the compliance requirements under the Privacy Shield are generally more stringent than under the Safe Harbor. The Privacy Shield is subject to annual review by the EU Commission. In October 2017, the EU Commission released its report and accompanying working document on the first annual review of the Privacy Shield, including recommendations on the functioning of the Privacy Shield that need to be improved by the US authorities. The Art. 29 Working Party (advisory body comprised of representatives of EU data protection authorities) issued in December 2017 a report concerning the first annual review of the functioning of the Privacy Shield in which it identified a number of significant concerns that need to be addressed by both the EU Commission and the U.S. authorities by May 25, 2018. The Art. 29 Working Party threatens to take legal action against the Privacy Shield adequacy decision if its concerns are not properly addressed within the given timeframe. Other methods for transferring personal data across the Atlantic are also facing legal scrutiny. In October 2017 the Irish High Court decided in a case concerning the validity of standard contractual clauses to refer certain questions to the European Court of Justice, or the ECJ, for a determination in a preliminary ruling. An adverse decision from the ECJ will impact how either we or our clients transfer personal data out of the EU. Further uncertainty exists with regard to data transfers in relation to the United Kingdom due to a referendum in which voters in the UK decided to withdraw from the European Union. Finally, the EU recently adopted the General Data Protection Regulation, or GDPR, which is the most comprehensive reform of data protection law in the EU's history. The GDPR, which will become applicable in May 2018, will significantly update and modify European data protection law, including extending its application to a wider range of non-EU entities, harmonizing data protection rules across EU member states, giving data subjects important new rights, and significantly increasing penalties for non-compliance.

In addition, as indicated above, we are also subject to Canada's Personal Information Protection and Electronic Documents Act, or PIPEDA, and the analogous provincial laws, which similarly impose data privacy and security obligations on our processing of personal data.

Any of these developments, and the cost of compliance, could harm our operations and financial results. Moreover, any non-compliance, or perceived non-compliance, with these obligations, could result in investigations or enforcement actions by applicable regulators, lawsuits by private parties, changes to our business practices, increased cost of operations, or declines in client growth, or may otherwise harm our business.

In addition to government activity, privacy advocacy groups and the technology and other industries are considering various new, additional or different self-regulatory standards that may place additional burdens on us. If the processing of information were to be curtailed in this manner, our solution may be less attractive, which may reduce demand for our solution and harm our business.

Risks Related to Ownership of Our Common Stock

Our stock price has been volatile, may continue to be volatile and may decline, including due to factors beyond our control.

The market price of our common stock has been volatile in the past and may fluctuate significantly in the future in response to numerous factors, many of which are beyond our control. During the three months ended March 31, 2018, the sale price per share of our common stock ranged from a low of $22.55 to a high of $32.47. Factors that may contribute to continuing volatility in the price of our common stock include:

- actual or anticipated fluctuations in our operating results;
- the financial projections we provide to the public, any changes in these projections or our failure to meet these projections;
- failure of securities analysts to initiate or maintain coverage of our company, changes in financial estimates by any securities analysts who follow our company, or our failure to meet these estimates or the expectations of investors;
- ratings changes by any securities analysts who follow our company;
- sales of our common stock by us or our significant stockholders, or the public announcement of same;

Table of Contents

- the assessment of our business or position in our market published in research and other reports;
- announcements by us or our competitors of significant technical innovations, financings, acquisitions, strategic partnerships, joint ventures or capital commitments;
- changes in operating performance and stock market valuations of other technology companies generally, or those in the software as a service industry in particular;
- price and volume fluctuations in the overall stock market, including as a result of trends in the U.S. or global economy;
- any major change in our board of directors or management;
- lawsuits threatened or filed against us;
- security breaches or incidents impacting our clients or their customers;
- legislation or regulation of our business, the internet and/or contact centers;
- loss of key personnel;
- new entrants into the contact center market, including the transition by providers of legacy on-premise contact center systems to cloud solutions, as well as cable and incumbent telephone companies and other well-capitalized competitors;
- new products or new sales by us or our competitors;
- the perceived or real impact of events that harm our direct competitors;
- developments with respect to patents or proprietary rights;
- general market conditions;
- distributions to limited partners, or block sales, by original venture capital investors; and
- other events or factors, including those resulting from war, incidents of terrorism or responses to these events, which could be unrelated to, or outside of, our control.

In addition, stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many technology companies. Stock prices of many technology companies have fluctuated in a manner unrelated or disproportionate to the operating performance of those companies. These and other factors may disproportionately impact the trading price of our common stock. In the past, stockholders have instituted securities class action litigation following periods of market volatility. If we were to become involved in securities litigation, it could subject us to substantial costs, divert resources and the attention of management from our business and harm our business, results of operations, financial condition, reputation and cash flows.

If securities or industry analysts discontinue publishing research or reports about our business, or publish negative reports about our business, our share price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about us or our business, our market and our competitors. We do not have any control over these analysts. If one or more of the analysts who cover us downgrade our shares or change their opinion of our shares, our share price would likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which could cause our share price or trading volume to decline.

Substantial future sales of shares of our common stock could cause the market price of our common stock to decline.

The market price of shares of our common stock could decline as a result of substantial sales of our common stock, particularly sales by our directors, executive officers and significant stockholders and persons to whom our shares are distributed by our significant stockholders or the perception in the market that holders of a large number of shares intend to sell their shares.

The future registration of shares of our common stock may cause our stock price to decline, even before such shares are actually sold in the market. We have also registered shares of common stock that we may issue under our employee equity incentive plans. These shares can be sold freely in the public market upon issuance.

We are unable to predict the effect that sales, or the perception that our shares may be available for sale, will have on the prevailing market price of our common stock.

Table of Contents

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of our company more difficult, limit attempts by our stockholders to replace or remove our current management and limit the market price of our common stock.

Provisions in our amended and restated certificate of incorporation and amended and restated bylaws may have the effect of delaying or preventing a change in control or changes in our management. Our amended and restated certificate of incorporation and amended and restated bylaws:

- provide that our board of directors is classified into three classes of directors;
- provide that stockholders may remove directors only for cause and only with the approval of holders of at least 66 $^2/_3$% of our then outstanding capital stock;
- provide that the authorized number of directors may be changed only by resolution of the board of directors;
- provide that all vacancies, including newly created directorships, may, except as otherwise required by law, be filled by the affirmative vote of a majority of directors then in office, even if less than a quorum;
- provide that our stockholders may not take action by written consent, and may only take action at annual or special meetings of our stockholders;
- provide that stockholders seeking to present proposals before a meeting of stockholders or to nominate candidates for election as directors at a meeting of stockholders must provide notice in writing in a timely manner, and also specify requirements as to the form and content of a stockholder's notice;
- restrict the forum for certain litigation against us to Delaware;
- do not provide for cumulative voting rights (therefore allowing the holders of a majority of the shares of common stock entitled to vote in any election of directors to elect all of the directors standing for election);
- provide that special meetings of our stockholders may be called only by the chairman of the board, our chief executive officer or the board of directors pursuant to a resolution adopted by a majority of the total number of authorized directors; and
- provide that stockholders will be permitted to amend our amended and restated bylaws only upon receiving at least 66$^2/_3$% of the votes entitled to be cast by holders of all outstanding shares then entitled to vote generally in the election of directors, voting together as a single class.

These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management. In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which generally prohibits a Delaware corporation from engaging in any of a broad range of business combinations with any "interested" stockholder for a period of three years following the date on which the stockholder became an "interested" stockholder.

The existence of these provisions could negatively affect the price of our common stock and limit opportunities for you to realize value in a corporate transaction.

Our amended and restated certificate of incorporation provides that the Court of Chancery of the State of Delaware is the sole and exclusive forum for substantially all disputes between us and our stockholders, which could limit our stockholders' ability to obtain a favorable judicial forum for disputes with us or our directors, officers or employees.

Our amended and restated certificate of incorporation provides that, unless we consent to the selection of an alternative forum, the Court of Chancery of the State of Delaware is the sole and exclusive forum for (1) any derivative action or proceeding brought on our behalf, (2) any action asserting a claim of breach of fiduciary duty owed by any of our directors, officers or other employees to us or to our stockholders, (3) any action asserting a claim arising pursuant to the Delaware General Corporation Law or (4) any action asserting a claim governed by the internal affairs doctrine. The choice of forum provision may limit a stockholder's ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers or other employees, which may discourage such lawsuits against us and our directors, officers and other employees. Alternatively, if a court were to find the choice of forum provision contained in our amended and restated certificate of incorporation to be inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions, which could harm our business, operating results and financial condition.

59

Table of Contents

We have never paid cash dividends and do not intend to pay dividends for the foreseeable future.

We have never declared or paid any cash dividends on our common stock. We currently intend to retain any future earnings and do not expect to pay any dividends in the foreseeable future. Any future determination to declare cash dividends will be made at the discretion of our board of directors, subject to applicable laws, and will depend on a number of factors, including our financial condition, results of operations, capital requirements, contractual restrictions, general business conditions and other factors that our board of directors may deem relevant. In addition, our Revolving Credit Facility prohibits us and our subsidiaries from, among other things, paying any dividends or making any other distribution or payment on account of our common stock. Accordingly, holders of our common stock must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investments.

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

Not applicable.

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

None.

Table of Contents

ITEM 6. Exhibits

Exhibit Number	Description
10.1*+	Offer Letter dated August 12, 2013 between the Registrant and Gaurav Passi
10.2+	Five9, Inc. 2018 Executive Bonus Plan (filed as Exhibit 10.14 to the Company's Annual Report on Form 10-K filed with the SEC on March 1, 2018 (File No. 001-36383) and incorporated by reference herein)
31.1*	Certification of Chief Executive Officer of Five9, Inc. Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2*	Certification of Chief Financial Officer of Five9, Inc. Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1**	Certification of Chief Executive Officer and Chief Financial Officer of Five9, Inc. Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Schema Linkbase Document
101.CAL*	XBRL Taxonomy Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Definition Linkbase Document
101.LAB*	XBRL Taxonomy Labels Linkbase Document
101.PRE*	XBRL Taxonomy Presentation Linkbase Document

* Filed herewith.
** Furnished herewith.
+ Indicates management contract.

Table of Contents

SIGNATURES

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

			Five9, Inc.
Date:	May 1, 2018	By:	/s/ Barry Zwarenstein
			Barry Zwarenstein
			Interim Chief Executive Officer and Chief Financial Officer
			(Principal Executive Officer, Principal Financial Officer and Principal Accounting Officer)