

Carbonite Inc  
Form 10-Q  
August 07, 2017  
Table of Contents

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

OR

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

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

Commission file number: 001-35264

CARBONITE, INC.

(Exact name of registrant as specified in its charter)

Delaware 33-1111329

(State or other jurisdiction of (I.R.S. Employer  
incorporation) Identification No.)

Two Avenue de Lafayette, Boston, Massachusetts 02111

(Address of principal executive offices, including ZIP code)

(617) 587-1100

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

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

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Exchange Act. "

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

As of July 31, 2017, there were 27,799,054 shares of the registrant's Common Stock, par value \$0.01 per share, outstanding.

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Table of Contents

CARBONITE, INC.

Table of Contents

|   | Page      |
|---|-----------|
| <u>PART I. FINANCIAL INFORMATION</u>  |           |
| Item 1. <u>Financial Statements (Unaudited)</u>   | <u>3</u>  |
| <u>Condensed Consolidated Balance Sheets as of June 30, 2017 and December 31, 2016</u>  | <u>3</u>  |
| <u>Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2017 and 2016</u>                  | <u>4</u>  |
| <u>Condensed Consolidated Statements of Comprehensive (Loss) Income for the three and six months ended June 30, 2017 and 2016</u> | <u>5</u>  |
| <u>Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2017 and 2016</u>                            | <u>6</u>  |
| <u>Notes to Condensed Consolidated Financial Statements</u>   | <u>7</u>  |
| Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>                              | <u>24</u> |
| Item 3. <u>Quantitative and Qualitative Disclosure About Market Risks</u>   | <u>35</u> |
| Item 4. <u>Controls and Procedures</u>  | <u>35</u> |
| <u>PART II. OTHER INFORMATION</u>   |           |
| Item 1. <u>Legal Proceedings</u>  | <u>36</u> |
| Item 1.A. <u>Risk Factors</u>   | <u>36</u> |
| Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>  | <u>37</u> |
| Item 3. <u>Defaults Upon Senior Securities</u>  | <u>37</u> |
| Item 4. <u>Mine Safety Disclosures</u>  | <u>37</u> |
| Item 5. <u>Other Information</u>  | <u>37</u> |
| Item 6. <u>Exhibits</u>   | <u>38</u> |
| <u>Signatures</u>   | <u>39</u> |

Table of Contents

## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

Carbonite, Inc.

Condensed Consolidated Balance Sheets

(Unaudited)

|   | June 30, 2017                     | December 31,<br>2016 |
|---|-----------------------------------|----------------------|
|   | (in thousands, except share data) |                      |
| <b>ASSETS</b>   |                                   |                      |
| Current assets:   |                                   |                      |
| Cash and cash equivalents   | \$ 125,099                        | \$ 59,152            |
| Trade accounts receivable, less allowances for doubtful accounts of \$1,717 and \$1,587   | 23,505                            | 16,639               |
| Prepaid expenses and other current assets   | 7,850                             | 7,325                |
| Restricted cash   | —                                 | 135                  |
| Total current assets  | 156,454                           | 83,251               |
| Property and equipment, net   | 27,798                            | 23,872               |
| Other assets  | 348                               | 157                  |
| Acquired intangible assets, net   | 45,924                            | 13,751               |
| Goodwill  | 74,082                            | 23,728               |
| Total assets  | \$ 304,606                        | \$ 144,759           |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                                   |                      |
| Current liabilities:  |                                   |                      |
| Accounts payable  | \$ 6,021                          | \$ 5,819             |
| Accrued expenses  | 20,631                            | 19,768               |
| Current portion of deferred revenue   | 102,224                           | 86,311               |
| Total current liabilities   | 128,876                           | 111,898              |
| Long-term debt, net of debt issuance costs  | 108,782                           | —                    |
| Deferred revenue, net of current portion  | 24,756                            | 21,280               |
| Other long-term liabilities   | 6,186                             | 5,747                |
| Total liabilities   | 268,600                           | 138,925              |
| Commitments and contingencies (Note 11)   |                                   |                      |
| Stockholders' equity:   |                                   |                      |
| Preferred stock, \$0.01 par value; 6,000,000 shares authorized; no shares issued  | —                                 | —                    |
| Common stock, \$0.01 par value; 45,000,000 shares authorized at June 30, 2017 and December 31, 2016; 29,761,326 shares issued and 27,792,968 shares outstanding at June 30, 2017; 28,545,089 shares issued and 27,394,024 shares outstanding at December 31, 2016 | 298                               | 285                  |
| Additional paid-in capital  | 224,815                           | 177,931              |
| Treasury stock, at cost (1,968,358 and 1,151,065 shares as of June 30, 2017 and December 31, 2016, respectively)  | (26,630)                          | (10,657)             |
| Accumulated other comprehensive income  | 1,650                             | 3,317                |
| Accumulated deficit   | (164,127)                         | (165,042)            |
| Total stockholders' equity  | 36,006                            | 5,834                |
| Total liabilities and stockholders' equity  | \$ 304,606                        | \$ 144,759           |

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

Table of ContentsCarbonite, Inc.  
Condensed Consolidated Statements of Operations  
(Unaudited)

|  | Three Months Ended<br>June 30,                     |            | Six Months Ended<br>June 30, |            |
|--|--|------------|------------------------------|------------|
|  | 2017   | 2016       | 2017                         | 2016       |
|  | (in thousands, except share and per share amounts) |            |                              |            |
| Revenue  | \$59,034   | \$ 53,435  | \$ 116,133                   | \$ 101,550 |
| Cost of revenue                                      | 18,311   | 15,864     | 35,666                       | 30,619     |
| Gross profit   | 40,723   | 37,571     | 80,467                       | 70,931     |
| Operating expenses:                                  |  |            |                              |            |
| Research and development                             | 10,927   | 8,380      | 21,254                       | 17,116     |
| General and administrative                           | 11,076   | 10,389     | 23,946                       | 21,809     |
| Sales and marketing                                  | 23,373   | 17,323     | 46,793                       | 34,205     |
| Restructuring charges                                | —  | 32         | —                            | 805        |
| Total operating expenses                             | 45,376   | 36,124     | 91,993                       | 73,935     |
| (Loss) income from operations                        | (4,653 )   | 1,447      | (11,526 )                    | (3,004 )   |
| Interest (expense) income, net                       | (2,239 )   | (97 )      | (2,441 )                     | (95 )      |
| Other income (expense), net                          | 915  | 100        | 1,195                        | (52 )      |
| (Loss) income before income taxes                    | (5,977 )   | 1,450      | (12,772 )                    | (3,151 )   |
| Provision (benefit) for income taxes                 | 403  | 290        | (13,987 )                    | 385        |
| Net (loss) income                                    | \$(6,380 )   | \$ 1,160   | \$ 1,215                     | \$(3,536 ) |
| Net (loss) income per common share:                  |  |            |                              |            |
| Basic  | \$(0.23 )  | \$ 0.04    | \$ 0.04                      | \$(0.13 )  |
| Diluted  | \$(0.23 )  | \$ 0.04    | \$ 0.04                      | \$(0.13 )  |
| Weighted-average number of common share outstanding: |  |            |                              |            |
| Basic  | 27,525,647   | 26,901,419 | 27,672,804                   | 26,977,919 |
| Diluted  | 27,525,647   | 27,012,361 | 28,354,616                   | 26,977,919 |

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

Table of Contents

Carbonite, Inc.

Condensed Consolidated Statements of Comprehensive (Loss) Income  
(Unaudited)

|  | Three Months<br>Ended<br>June 30,<br>2017 |          | Six Months<br>Ended<br>June 30,<br>2016 |            |
|--|---|----------|---|------------|
|  | 2017                                      | 2016     | 2017                                    | 2016       |
|  | (in thousands)                            |          |   |            |
| Net (loss) income                        | \$ (6,380)                                | \$ 1,160 | \$ 1,215                                | \$ (3,536) |
| Other comprehensive (loss) income:       |   |          |   |            |
| Foreign currency translation adjustments | (1,423 )                                  | 691      | (1,667 )                                | 118        |
| Total other comprehensive (loss) income  | (1,423 )                                  | 691      | (1,667 )                                | 118        |
| Total comprehensive (loss) income        | \$ (7,803)                                | \$ 1,851 | \$ (452 )                               | \$ (3,418) |

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

Table of Contents

Carbonite, Inc.

Condensed Consolidated Statements of Cash Flows  
(Unaudited)

|   | Six Months Ended<br>June 30, |            |
|---|------------------------------|------------|
|   | 2017                         | 2016       |
|   | (in thousands)               |            |
| Operating activities  |                              |            |
| Net income (loss)   | \$1,215                      | \$(3,536)  |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: |                              |            |
| Depreciation and amortization   | 10,392                       | 8,378      |
| (Gain) loss on disposal of equipment  | (928)                        | ) 468      |
| Stock-based compensation expense  | 5,965                        | 4,498      |
| Benefit for deferred income taxes   | (14,964)                     | ) (169)    |
| Non-cash interest expense related to amortization of debt discount                        | 1,466                        | —          |
| Other non-cash items, net   | (249)                        | ) 280      |
| Changes in assets and liabilities:  |                              |            |
| Accounts receivable   | (89)                         | ) (13,458) |
| Prepaid expenses and other current assets   | (58)                         | ) (2,026)  |
| Other assets  | (137)                        | ) 1        |
| Accounts payable  | 627                          | (4,113)    |
| Accrued expenses  | (2,340)                      | ) 3,841    |
| Other long-term liabilities   | 120                          | (353)      |
| Deferred revenue  | 9,548                        | 4,516      |
| Net cash provided by (used in) operating activities                                       | 10,568                       | (1,673)    |
| Investing activities  |                              |            |
| Purchases of property and equipment   | (10,039)                     | ) (2,809)  |
| Proceeds from sale of property and equipment  | 560                          | —          |
| Proceeds from maturities of marketable securities and derivatives                         | 370                          | 1,000      |
| Purchases of marketable securities and derivative settlements                             | (2,433)                      | ) (1,476)  |
| Proceeds from sale of businesses  | 295                          | —          |
| Payment for acquisition, net of cash acquired   | (60,198)                     | ) (11,625) |
| Net cash used in investing activities   | (71,445)                     | ) (14,910) |
| Financing activities  |                              |            |
| Proceeds from exercise of stock options   | 3,337                        | 381        |
| Repurchase of common stock  | (15,973)                     | ) (4,626)  |
| Proceeds from long-term borrowings, net of debt issuance costs                            | 177,797                      | —          |
| Payments on long-term borrowings  | (39,200)                     | ) —        |
| Net cash provided by (used in) financing activities                                       | 125,961                      | (4,245)    |
| Effect of currency exchange rate changes on cash  | 863                          | 95         |
| Net increase (decrease) in cash and cash equivalents                                      | 65,947                       | (20,733)   |
| Cash and cash equivalents, beginning of period  | 59,152                       | 63,936     |
| Cash and cash equivalents, end of period  | \$125,099                    | \$43,203   |
| Supplemental disclosure of cash flow information  |                              |            |
| Cash paid for income taxes  | \$616                        | \$480      |
| Supplemental disclosure of non-cash investing and financing activities:                   |                              |            |
| Capitalization of stock-based compensation  | \$112                        | \$30       |
| Acquisition of property and equipment included in accounts payable and accrued expenses   | \$(1,050)                    | ) \$(63)   |
| Issuance of common stock for acquisition  | \$5,733                      | \$—        |

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

6

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Table of Contents

Carbonite, Inc.

Notes to Condensed Consolidated Financial Statements  
(Unaudited)

1. Nature of Business

Carbonite, Inc. ("we" or the "Company") was incorporated in the State of Delaware on February 10, 2005 and is a provider of data protection solutions for businesses and the IT professionals who serve them. The Company's product suite, including EVault, Inc. ("EVault") and Double-Take Software, Inc. ("Double-Take"), provides a full complement of backup, disaster recovery and high availability solutions for any size business in locations around the world, all supported by a secure global infrastructure.

2. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") and include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts and transactions between the Company and its subsidiaries have been eliminated in consolidation.

The accompanying unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the United States Securities and Exchange Commission ("SEC"), the instructions to Form 10-Q, and the provisions of Regulation S-X pertaining to interim financial statements. Accordingly, certain information and footnote disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. These condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and the notes thereto, included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016, as filed with the SEC on March 16, 2017.

In the opinion of management, the condensed consolidated financial statements reflect all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the Company's financial position for the periods presented. The results for the periods presented are not necessarily indicative of future results.

There have been no material changes to the Company's significant accounting policies previously presented in our Annual Report on Form 10-K filed with the SEC on March 16, 2017.

Recently Adopted Accounting Standards

In March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting ("ASU 2016-09"). The amendments in this ASU involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. For public entities, ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years, with earlier adoption permitted for all entities. On January 1, 2017, the Company adopted ASU 2016-09. In connection with the adoption of this standard, the Company changed its accounting policy to record actual forfeitures as they occur, rather than estimating forfeitures by applying a forfeiture rate. As this policy change was applied prospectively, prior periods have not been adjusted. As a result of adoption, the Company recorded an immaterial impact to retained earnings and additional paid in capital. The Company retrospectively adjusted the classification of excess tax benefits on the statement of cash flow from financing to operating; the effect was immaterial.

In May 2017, the FASB issued ASU 2017-09, Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting ("ASU 2017-09"). The amendments in ASU 2017-09 clarify that modification accounting is required only if the fair value, the vesting conditions, or the classification of the award (as equity or liability) changes as a result of the changes in terms or conditions. ASU 2017-09 is effective for fiscal years beginning after December 15, 2017. Early application is permitted and prospective application is required. As early adoption is permitted, the Company adopted this standard in the second quarter of 2017, which did not have a material impact on the consolidated financial statements.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"), which updated guidance and disclosure requirements for

7

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Table of Contents

recognizing revenue. The new revenue recognition standard provides a five-step analysis of transactions to determine when and how revenue is recognized. The revenue standard is based on the principle that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In March 2016, the FASB issued an amendment to the standard, ASU 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net), which clarifies the implementation guidance on principal versus agent considerations. In April 2016, the FASB issued an additional amendment to the standard, ASU 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing (“ASU 2016-10”), which clarifies the guidance on identifying performance obligations and the implementation guidance on licensing. The collective guidance will be effective for the Company on January 1, 2018, with early adoption permitted. The guidance may be applied retrospectively to each prior period presented (full retrospective) or retrospectively with the cumulative effect recognized as of the date of initial adoption (modified retrospective). The Company will adopt ASU 2014-09 in the first quarter of 2018. The Company currently expects to apply the modified retrospective transition method. While the Company continues to assess the potential impact of these standards on its consolidated financial statements and disclosures, the Company has begun identifying necessary changes to its systems, processes, and internal controls. The Company continues to refine its implementation timeline which is expected to last the duration of 2017.

In February 2016, the FASB issued ASU 2016-02, Leases (“ASU 2016-02”). ASU 2016-02 requires lessees to recognize the assets and liabilities on their balance sheet for the rights and obligations created by most leases and continue to recognize expenses on their income statements over the lease term. It will also require disclosures designed to give financial statement users information on the amount, timing, and uncertainty of cash flows arising from leases. The guidance is effective for annual reporting periods beginning after December 15, 2018 and interim periods within those fiscal years, with early adoption permitted. The Company is currently evaluating the effect of the standard on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments (“ASU 2016-13”). ASU 2016-13 is intended to improve financial reporting by requiring timelier recognition of credit losses for financial instruments held by financial institutions and other organizations. ASU 2016-13 is effective for fiscal years, and interim periods within, beginning after December 15, 2019. Early adoption is permitted. The Company is currently evaluating the effect of the standard on its consolidated financial statements.

In October 2016, the FASB issued ASU 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory (“ASU 2016-16”). The purpose of ASU 2016-16 is to simplify the income tax accounting of an intra-entity transfer of an asset other than inventory and to record its effect when the transfer occurs. The guidance is effective for annual reporting periods beginning after December 15, 2017, including interim reporting periods within those annual reporting periods and early adoption is permitted. The Company is currently evaluating the effect of the standard on its consolidated financial statements.

On November 17, 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (“ASU 2016-18”). ASU 2016-18 requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents and amounts generally described as restricted cash or restricted cash equivalents. Entities will also be required to reconcile such total to amounts on the balance sheet and disclose the nature of the restrictions. The guidance is effective for annual reporting periods beginning after December 15, 2017 and interim periods within those fiscal years. The Company is currently evaluating the effect of the standard on its consolidated financial statements, but does not expect it to have a material impact.

In January 2017, the FASB issued ASU No. 2017-01, Clarifying the Definition of a Business (“ASU 2017-01”). The amendments in this ASU clarify the requirements for a set of activities to be considered a business and narrows the

definition of an output. ASU 2017-01 is effective for fiscal years, and interim periods within, beginning after December 15, 2017. Early adoption is permitted. A reporting entity must apply the amendments in ASU 2017-01 using a prospective approach. The Company is currently evaluating the effect of the standard on its consolidated financial statements, but does not expect it to have a material impact.

In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment. The standard eliminates the second step in the goodwill impairment test which requires an entity to determine the implied fair value of the reporting unit's goodwill. The standard is effective for annual and interim goodwill impairment tests conducted in fiscal years beginning after December 15, 2019, with early adoption permitted. The Company is currently evaluating the effect of the standard on its consolidated financial statements.

In February 2017, the FASB issued ASU 2017-05, Other Income - Gains and Losses from the Derecognition of Nonfinancial Assets ("ASU 2017-05"). The amendments in ASU 2017-05 define the term in substance nonfinancial asset. The

Table of Contents

amendments further clarify that if substantially all of the fair value of the assets that are promised to the counterparty in a contract is concentrated in nonfinancial assets, then all of the financial assets promised to the counterparty are in substance nonfinancial assets. For public entities, ASU 2017-05 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years, with earlier adoption permitted for all entities. The Company is currently assessing the effect of the standard on its consolidated financial statements.

## 3. Net (Loss) Income Per Share

Basic (loss) income per share is calculated by dividing the net (loss) income by the weighted average number of common shares outstanding during the period. Diluted net (loss) income per share is calculated by dividing net (loss) income by the sum of the weighted average number of common shares and potentially dilutive securities outstanding during the period using the treasury stock method. For the periods in which the Company incurred a net loss, the effect of the Company's outstanding common stock equivalents were not included in the calculation of diluted loss per share as they were anti-dilutive. Accordingly, basic and diluted net loss per share for those periods were identical.

The following table sets forth the computation of basic and diluted net (loss) income per share:

|   | Three Months                             |         | Six Months     |           |
|---|--|---------|----------------|-----------|
|   | Ended June 30,                           |         | Ended June 30, |           |
|   | 2017                                     | 2016    | 2017           | 2016      |
|   | (in thousands, except per share amounts) |         |                |           |
| Numerator:  |  |         |                |           |
| Net (loss) income                                 | \$(6,380)                                | \$1,160 | \$1,215        | \$(3,536) |
| Denominator:                                      |  |         |                |           |
| Weighted average common shares outstanding, basic | 27,526                                   | 26,901  | 27,673         | 26,978    |
| Effect of potential dilutive common shares        | —  | 111     | 682            | —         |
| Weighted average shares outstanding, diluted      | 27,526                                   | 27,012  | 28,355         | 26,978    |
| Basic net (loss) income per share                 | \$(0.23 )                                | \$0.04  | \$0.04         | \$(0.13 ) |
| Diluted net (loss) income per share               | \$(0.23 )                                | \$0.04  | \$0.04         | \$(0.13 ) |

The following options to purchase common shares and restricted stock units have been excluded from the computation of diluted net (loss) income per share because they had an anti-dilutive impact (in thousands):

|                                   | Three    |       | Six      |       |
|-----------------------------------|----------|-------|----------|-------|
|                                   | Months   |       | Months   |       |
|                                   | Ended    |       | Ended    |       |
|                                   | June 30, |       | June 30, |       |
|                                   | 2017     | 2016  | 2017     | 2016  |
| Options to purchase common shares | 36       | 1,622 | 36       | 1,974 |
| Restricted stock units            | 332      | 1,298 | 559      | 2,006 |
| Total                             | 368      | 2,920 | 595      | 3,980 |

The Company has outstanding convertible notes issued in April 2017 that have the potential to dilute basic earnings per share in future periods which have been excluded from the calculation of diluted earnings per share. As the closing price of the Company's common stock on June 30, 2017 did not exceed the conversion price on the notes of \$25.84 and the Company has the ability and intent to settle the notes in cash, there was no impact on diluted earnings per share during the three and six months ended June 30, 2017.

## 4. Fair Value of Financial Instruments

## Derivative Instruments

## Non-designated Foreign Currency Contracts

The Company uses foreign currency forward contracts as part of its strategy to manage exposure related to Euro denominated intercompany monetary assets and liabilities. The Company has not designated these forward contracts

as hedging instruments pursuant to ASC 815, Derivatives and Hedging. Accordingly, the Company recorded the fair value of these contracts at the end of each reporting period in the consolidated balance sheets, with changes in the fair value recorded in

9

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Table of Contents

earnings as other income (expense), net in the consolidated statements of operations. Cash flows from the settlement of these non-designated foreign currency contracts are reported in cash flows from investing activities. These currency forward contracts are entered into for periods consistent with currency transaction exposures, generally less than one year. At June 30, 2017 and December 31, 2016, the Company had outstanding contracts with a total notional value of \$43.8 million and \$37.7 million, respectively.

The following table provides a quantitative summary of the fair value of derivative instruments not designated as hedging instruments as of June 30, 2017 and December 31, 2016 (in thousands):

| Description                               | Balance Sheet Classification              | Fair Value    |                   |
|---|---|---------------|-------------------|
|   |   | June 30, 2017 | December 31, 2016 |
| <b>Derivative Assets:</b>                 |   |               |                   |
| <b>Non-Designated Hedging Instruments</b> |   |               |                   |
| Foreign currency contracts                | Prepaid expenses and other current assets | \$25          | \$ 380            |
| <b>Total Derivative Assets</b>            |   | <b>\$25</b>   | <b>\$ 380</b>     |
| <b>Derivative Liabilities:</b>            |   |               |                   |
| <b>Non-Designated Hedging Instruments</b> |   |               |                   |
| Foreign currency contracts                | Accrued expenses                          | \$812         | \$ —              |
| <b>Total Derivative Liabilities</b>       |   | <b>\$812</b>  | <b>\$ —</b>       |

The following table summarizes the losses related to derivative instruments not designated as hedging instruments for the three and six month periods ended June 30, 2017 and 2016 (in thousands):

| Location in Statement of Operations                    | Three Months Ended June 30, |         | Six Months Ended June 30, |         |
|--|-----------------------------|---------|---------------------------|---------|
|  | 2017                        | 2016    | 2017                      | 2016    |
| Foreign currency contracts Other income (expense), net | \$(2,820)                   | \$1,042 | \$(3,231)                 | \$(715) |

**Other Fair Value Measurements and Disclosures**

The Company applies the guidance in ASC 820, Fair Value Measurements and Disclosures, (“ASC 820”), which provides that fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, ASC 820 establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Other inputs that are observable directly or indirectly, such as quoted prices for similar assets and liabilities or market corroborated inputs.

Level 3: Unobservable inputs are used when little or no market data is available, which requires the Company to develop its own assumptions about how market participants would value the assets or liabilities. The fair value hierarchy gives the lowest priority to Level 3 inputs.

In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible in its assessment of fair value.

Table of Contents

The Company's assets and liabilities that are measured at fair value on a recurring basis, by level, within the fair value hierarchy are summarized as follows (in thousands):

|                                     | June 30, 2017 |         |         |           | December 31, 2016 |         |         |           |
|-------------------------------------|---------------|---------|---------|-----------|-------------------|---------|---------|-----------|
|                                     | Level 1       | Level 2 | Level 3 | Total     | Level 1           | Level 2 | Level 3 | Total     |
| Assets:                             |               |         |         |           |                   |         |         |           |
| Cash equivalents—money market funds | \$80,866      | \$ —    | \$ —    | —\$80,866 | \$20,728          | \$ —    | \$ —    | —\$20,728 |
| Foreign currency exchange contracts | —             | 25      | —       | 25        | —                 | 380     | —       | 380       |
| Total                               | \$80,866      | \$ 25   | \$ —    | —\$80,891 | \$20,728          | \$ 380  | \$ —    | —\$21,108 |
| Liabilities:                        |               |         |         |           |                   |         |         |           |
| Foreign currency exchange contracts | —             | 812     | —       | 812       | —                 | —       | —       | —         |
| Total                               | \$—           | \$ 812  | \$ —    | —\$812    | \$—               | \$ —    | \$ —    | —\$—      |

The Company's investments in money market funds are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices. Our marketable securities and foreign currency exchange contracts are classified as Level 2 within the fair value hierarchy as they are valued using professional pricing sources for identical or comparable instruments, rather than direct observations of quoted prices in active markets. No assets or liabilities are classified as Level 3 within the fair value hierarchy.

The Company estimates the fair value of its 2.50% convertible senior notes (the "Convertible Notes") using quoted market prices of the Convertible Notes in an inactive market on the last trading day of the reporting period and has been classified as Level 2 within the fair value hierarchy. The principal amount, carrying value of the Convertible Notes (the carrying value excludes the equity component of the Convertible Notes classified in equity) and related estimated fair value of the Company's Convertible Notes reported in the condensed consolidated balance sheet as of June 30, 2017 are as follows (in thousands):

|                   | June 30, 2017 |                |            |
|-------------------|---------------|----------------|------------|
|                   | Principal     | Carrying Value | Fair Value |
| Convertible notes | \$ 143,750    | \$ 108,783     | \$ 159,383 |

#### Non-Recurring Fair Value Measures

Certain non-financial assets and liabilities are measured at fair value on a non-recurring basis and are subject to fair value adjustments in certain circumstances, such as acquired assets and liabilities. For assets and liabilities measured on a non-recurring basis during the period, accounting guidance requires quantitative disclosures about the fair value measurements separately for each major category.

## 5. Acquisitions

### 2017 Acquisition

On January 31, 2017, the Company completed the acquisition of all the outstanding capital stock of Double-Take for a purchase price of \$65.9 million, which was comprised of \$59.7 million in cash paid at closing, net of cash acquired, 332,326 shares of our common stock with a fair value of \$5.7 million and the working capital payment of \$0.5 million. The working capital settlement was paid in June 2017. Double-Take develops, sells, and supports affordable software that allows IT organizations of all sizes to move, manage, protect, and recover workloads across any distance and any combination of physical and virtual server environments. Double-Take's products and services are marketed and sold worldwide through their direct sales force and a network of business partners and distributors. In connection with the acquisition of Double-Take, the Company negotiated a transition services agreement ("TSA") to cover certain



consulting, technology and accounting services for up to nine months post close. The Company has incurred approximately \$0.9 million to date. The acquisition of Double-Take has been accounted for as a business combination and, in accordance with ASC 805, Business Combinations ("ASC 805"), the Company has recorded the assets acquired and liabilities assumed at their respective fair values as of the acquisition dates.

Table of Contents

The Company also entered into a registration rights agreement ("Registration Rights Agreement"), whereby the Company agreed to register, on behalf of the sellers, the shares of common stock issued at closing. Pursuant to the terms in the Registration Rights Agreement, the Company filed a resale Form S-3 registration statement with the SEC that was declared effective on May 4, 2017.

The purchase price allocation is considered preliminary, and additional adjustments may be recorded during the allocation period in accordance with the FASB's guidance regarding business combinations. The purchase price allocation will be finalized as the Company receives additional information relevant to the acquisition, including the final valuation and reconciliation of the assets purchased, including tangible and intangible assets, and liabilities assumed. During the second quarter of 2017, the Company recorded a measurement period adjustment in our condensed consolidated balance sheet. The measurement period adjustment was recorded as a \$0.3 million decrease to goodwill, with an offsetting decrease to deferred tax liabilities of \$0.2 million and a decrease to other non-current liabilities of \$0.1 million. The following table summarizes the preliminary purchase price allocation, including the measurement period adjustments recorded in the second quarter of 2017 (in thousands):

Fair value of consideration transferred:

|                                   |          |
|-----------------------------------|----------|
| Cash, net of cash acquired        | \$59,740 |
| Fair value of equity instruments  | 5,733    |
| Working capital payment           | 458      |
| Fair value of total consideration | \$65,931 |

Fair value of assets acquired and liabilities assumed:

|                                  |           |
|----------------------------------|-----------|
| Accounts receivable              | \$6,058   |
| Prepaid and other current assets | 158       |
| Property and equipment           | 428       |
| Other long-term assets           | 42        |
| Intangible assets                | 36,700    |
| Goodwill                         | 49,473    |
| Total assets acquired            | 92,859    |
| Accounts payable                 | (636 )    |
| Accrued liabilities              | (2,156 )  |
| Deferred revenues                | (9,100 )  |
| Deferred tax liability           | (14,918 ) |
| Other non-current liabilities    | (118 )    |
| Net assets acquired              | \$65,931  |

The Company engaged a third-party valuation firm to assist in the valuation of intangible assets consisting of developed technology, customer relationships, and the Double-Take trade name as well as in the valuation of deferred revenue. The estimated fair values of intangibles assets of \$36.7 million, and deferred revenue of \$9.1 million, were developed by management based on their estimates, assumptions and acquisition history including reports from the third-party valuation firm. The estimated fair values of the intangible assets and deferred revenue are supported by valuations completed by management which were finalized in June 2017. The long-term deferred taxes of \$14.9 million are primarily related to temporary differences associated with the fair value allocations of intangible assets, deferred revenue, fixed assets, and certain operating accruals. The fair values of the remaining Double-Take assets and liabilities noted above approximate their carrying values at January 31, 2017.

In connection with the acquisition of Double-Take, goodwill of \$49.5 million was recognized for the excess purchase price over the fair value of the net assets acquired. The goodwill recorded in connection with this transaction is primarily related to revenue and cash flow projections associated with future technologies and new customer relationships. Goodwill from the acquisition of Double-Take is included within the Company's one reporting unit and will be included in the annual review for impairment. Goodwill is not deductible for tax purposes as this acquisition was a stock purchase.

The significant intangible assets identified in the purchase price allocation discussed above include developed technology, trade names and customer relationships, which are amortized over their estimated useful lives based on the pattern of

12

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Table of Contents

consumption of the economic benefits or, if that pattern cannot be readily determined, on a straight-line basis. Developed technology consists of products that have reached technological feasibility and trade names represent acquired company and product names. To value the developed technology asset, the Company utilized the income approach, specifically a discounted cash-flow method known as the multi-period excess earnings method. The trade name intangible was valued using a relief from royalty method, which considers both the market approach and the income approach. Customer relationships represent the underlying relationships with certain customers to provide ongoing services for products sold. The Company utilized the replacement cost/lost profits methodology to derive the fair value of the customer relationships. The Company utilized accounting guidance related to intangible assets which lists the pertinent factors to be considered when estimating the useful life of an intangible asset. These factors include, in part, a review of the expected use by the Company of the assets acquired, the expected useful life of another asset (or group of assets) related to the acquired assets and legal, regulatory or other contractual provisions that may limit the useful life of an acquired asset.

The following table presents the estimated fair values and useful lives of the identifiable intangible assets acquired and risk-adjusted discount rates used in the valuation:

|                                      | Amount         | Weighted Average Useful Life | Risk-Adjusted Discount Rates used in Valuation |
|--------------------------------------|----------------|------------------------------|--|
|                                      | (in thousands) | (in years)                   |  |
| Developed technology                 | \$ 29,900      | 5                            | 13.5%  |
| Customer relationships               | 4,900          | 6                            | 12.0%  |
| Trade names                          | 1,900          | 8                            | 12.0%  |
| Total identifiable intangible assets | \$ 36,700      |                              |  |

In the three months ended June 30, 2017 and 2016, acquisition-related expenses were \$0.7 million and \$0.5 million, respectively. In the six months ended June 30, 2017 and 2016, acquisition-related expenses were \$3.7 million and \$3.9 million respectively. Acquisition-related expenses have been included primarily in general and administrative expenses in the condensed consolidated statements of operations. The Company's prior year acquisition costs relate to the acquisition of certain assets of EVault. The Company determined that disclosing the amount of Double-Take related revenue and expenses included in the condensed consolidated statements of operations is impracticable as certain operations were integrated into the operations of the Company. Furthermore, the Company operates as a one reportable segment and does not consider Double-Take a separate reporting segment.

#### Pro Forma Financial Information

The following unaudited pro forma information presents the condensed consolidated results of operations of the Company and Double-Take for the three and six months ended June 30, 2016 as if the acquisition of Double-Take had been completed on January 1, 2016. These pro forma condensed consolidated financial results have been prepared for comparative purposes only and include certain adjustments that reflect pro forma results of operations, such as increased amortization for the fair value of acquired intangible assets, fair value adjustment for deferred revenue, elimination of interest expense with a promissory note due to the parent company, and adjustments relating to the tax effect of combining the Carbonite and Double-Take businesses.

The unaudited pro forma results do not reflect any operating efficiencies or potential cost savings which may result from the consolidation of the operations of the Company and Double-Take. Accordingly, these unaudited pro forma results are presented for informational purposes only and are not necessarily indicative of the results of operations that actually would have been achieved had the acquisition occurred as of January 1, 2016, nor are they intended to represent or be indicative of future results of operations (in thousands):

|        |        |
|--------|--------|
| Three  | Six    |
| Months | Months |

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|   | Ended<br>June 30,<br>2016 | Ended<br>June 30,<br>2016 |
|---|---------------------------|---------------------------|
| Revenue   | \$ 61,821                 | \$ 118,748                |
| Net loss  | \$ (1,859 )               | \$ (9,876 )               |
| Basic and diluted net loss per share  | \$ (0.07 )                | \$ (0.36 )                |
| Weighted-average number of common shares used in computing basic and diluted net loss per share | 27,233,745                | 27,310,245                |

13

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Table of Contents

## 2016 Acquisition

On January 13, 2016, the Company completed the acquisition of the North American cloud-based business continuity and disaster recovery assets of EVault and the acquisition of the assets used in the European Union operations of EVault was completed on March 31, 2016. The Company acquired EVault to offer business continuity and disaster recovery solutions designed for SMBs and small enterprises, including EVault Cloud Backup and Recovery, EVault Backup and Recovery Appliance and EVault Cloud Resiliency Services DRaaS offering.

The acquisition of EVault has been accounted for as a business combination and, in accordance with ASC 805, the Company has recorded the assets acquired and liabilities assumed at their respective fair values as of the acquisition dates.

In connection with the acquisition of EVault, the Company negotiated a transition services agreement ("EVault TSA") that provides a credit to be used against future services provided under the terms of the agreement. The Company estimated the fair value of the EVault TSA credit to be \$2.4 million and accounted for it as a reduction in consideration transferred in the purchase price allocation. The EVault TSA credit was recorded in prepaid expenses and other current assets on the consolidated balance sheet as of the acquisition date. The EVault TSA credit was fully expensed in 2016, and as such, there is no remaining balance of the EVault TSA credit on the consolidated balance sheet as of June 30, 2017.

The following tables summarize the purchase price allocation (in thousands):

Fair value of consideration transferred:

|  |          |
|--|----------|
| Cash   | \$14,000 |
| Fair value of prepaid EVault TSA                       | (2,375 ) |
| Fair value of total acquisition consideration          | \$11,625 |
| Fair value of assets acquired and liabilities assumed: |          |
| Prepaid expenses                                       | \$1,330  |
| Property and equipment                                 | 6,776    |
| Intangible assets                                      | 9,150    |
| Other long-term assets                                 | 564      |
| Goodwill   | 989      |
| Total assets acquired                                  | 18,809   |
| Deferred revenue                                       | (6,830 ) |
| Accrued liabilities                                    | (354 )   |
| Net assets acquired                                    | \$11,625 |

The significant intangible assets identified in the purchase price allocation discussed above include developed technology, trade names and customer relationships, which are amortized over their respective useful lives on a straight line basis. Developed technology consists of products that have reached technological feasibility and trade names represent acquired company and product names. To value the developed technology asset, the Company utilized the income approach, specifically a discounted cash-flow method known as the multi-period excess earnings method. The trade name intangible was valued using a relief from royalty method, which considers both the market approach and the income approach. Customer relationships represent the underlying relationships with certain customers to provide ongoing services for products sold. The Company utilized the replacement cost/lost profits methodology to derive the fair value of the customer relationships.



Table of Contents

The following table presents the estimated fair values and useful lives of the identifiable intangible assets acquired and risk-adjusted discount rates used in the valuation:

|   | Amount<br>(in thousands) | Weighted Average Useful<br>Life<br>(in years) | Risk-Adjusted Discount Rates used in<br>Valuation |
|---|--------------------------|---|---|
| Developed technology                    | \$ 5,650                 | 4   | 15.0%   |
| Customer relationships                  | 2,500                    | 6   | 14.0%   |
| Trade names                             | 1,000                    | 7   | 14.0%   |
| Total identifiable intangible<br>assets | \$ 9,150                 |   |   |

## 6. Goodwill and Acquired Intangible Assets

As of June 30, 2017 and December 31, 2016, the carrying amount of goodwill was \$74.1 million and \$23.7 million, respectively. The following is a rollforward of our goodwill balance (in thousands):

|                                  | Goodwill |
|----------------------------------|----------|
| Balance as of December 31, 2016  | \$23,728 |
| Goodwill acquired (1)            | 49,473   |
| Goodwill divested                | (27 )    |
| Effect of foreign exchange rates | 908      |
| Balance as of June 30, 2017      | \$74,082 |

(1) During the second quarter of 2017, goodwill was revised to reflect a purchase accounting measurement period adjustment related to the Double-Take acquisition. See Note 5—Acquisitions for additional information.

Purchased intangible assets consist of the following (in thousands):

|                        | Weighted-<br>Average<br>Estimated<br>Useful Life<br>(in years) | June 30, 2017              |                             |                          | December 31, 2016          |                             |                          |
|------------------------|--|----------------------------|-----------------------------|--------------------------|----------------------------|-----------------------------|--------------------------|
|                        |  | Gross<br>Carrying<br>Value | Accumulated<br>Amortization | Net<br>Carrying<br>Value | Gross<br>Carrying<br>Value | Accumulated<br>Amortization | Net<br>Carrying<br>Value |
| Developed technology   | 5.1  | \$42,866                   | \$ 7,958                    | \$ 34,908                | \$ 13,627                  | \$ 5,016                    | \$ 8,611                 |
| Customer relationships | 6.4  | 10,643                     | 2,587                       | 8,056                    | 6,056                      | 2,170                       | 3,886                    |
| Trade names            | 7.5  | 3,651                      | 691                         | 2,960                    | 1,710                      | 456                         | 1,254                    |
| Non-compete agreements | 3.0  | 230                        | 230                         | —                        | 380                        | 380                         | —                        |
| Total                  | 5.5  | \$57,390                   | \$ 11,466                   | \$ 45,924                | \$ 21,773                  | \$ 8,022                    | \$ 13,751                |

The Company recorded amortization expense of \$2.7 million and \$1.0 million for the three month periods ended June 30, 2017 and 2016, respectively; and \$4.7 million and \$2.0 million for the six month periods ended June 30, 2017 and 2016, respectively. Amortization relating to developed technology is recorded within cost of revenue, amortization of customer relationships is recorded within sales and marketing expenses, and amortization of trade names and non-compete agreements is recorded within general and administrative expenses.





Table of Contents

Future estimated amortization expense of acquired intangibles as of June 30, 2017 is as follows (in thousands):

|                   |          |
|-------------------|----------|
| Remainder of 2017 | \$5,336  |
| 2018              | 10,654   |
| 2019              | 10,611   |
| 2020              | 9,028    |
| 2021              | 7,850    |
| Thereafter        | 2,445    |
|                   | \$45,924 |

## 7. Accrued Expenses

Accrued expenses consist of the following (in thousands):

|  | June 30, December |           |
|--|-------------------|-----------|
|  | 2017              | 31, 2016  |
| Accrued compensation                     | \$9,092           | \$ 9,919  |
| Accrued consulting and professional fees | 2,697             | 2,342     |
| Accrued marketing                        | 1,543             | 896       |
| Accrued tax liabilities                  | 1,303             | 2,267     |
| Accrued facilities                       | 1,090             | 1,033     |
| Accrued interest                         | 859               | —         |
| Accrued derivative liability             | 812               | —         |
| Accrued other expenses                   | 3,235             | 3,311     |
| Total accrued expenses                   | \$20,631          | \$ 19,768 |

## 8. Stockholders' Equity

## Share Repurchase Program

On May 11, 2015, the Company's Board of Directors authorized a \$20.0 million share repurchase program, effective from May 15, 2015 through May 15, 2018. On March 22, 2017, the Company's Board of Directors authorized an increase to the share repurchase program to an aggregate amount of \$30.0 million. Share repurchases are made from time-to-time in the open market, in privately negotiated transactions or otherwise, in accordance with applicable securities laws and regulations. The timing and amount of any share repurchases are determined by the Company's management based on an evaluation of market conditions, the trading price of the stock, and other factors.

The Company made the following repurchases under the program during the three and six months ended June 30, 2017 and 2016:

|                                    | Three                     |                |         |
|------------------------------------|---------------------------|----------------|---------|
|                                    | Months                    | Six Months     |         |
|                                    | Ended                     | Ended June 30, |         |
|                                    | June 30,                  | 2017           | 2016    |
|                                    | 2016                      | 2017           | 2016    |
|                                    | (total cost, in millions) |                |         |
| Number of shares repurchased       | —136,536                  | 767,400        | 574,118 |
| Average repurchase price per share | \$— 9.53                  | \$ 19.50       | \$ 7.81 |
| Total cost                         | \$— 1.3                   | \$ 15.0        | \$ 4.5  |

At June 30, 2017, approximately \$5.2 million remained available under the Company's share repurchase program.

Table of Contents

## 9. Stock-based Awards

The Company's 2005 Stock Incentive Plan (the "2005 Plan") provided for granting of incentive stock options, non-qualified options, restricted stock, or other awards to the Company's employees, officers, directors, and outside consultants up to an aggregate of 3,601,551 shares of the Company's common stock. In conjunction with the effectiveness of the 2011 Equity Award Plan (the "2011 Plan"), the Company's Board of Directors voted that no further stock options or other equity-based awards would be granted under the 2005 Plan.

The 2011 Plan provides for the issuance of stock options, restricted stock, restricted stock units, and other stock-based awards to the employees, officers, directors, and consultants of the Company or its subsidiaries. In connection with the approval of the 2011 Plan, the Company reserved 1,662,000 shares of common stock for issuance thereunder. On January 1<sup>st</sup> of each year, beginning January 1, 2012, the number of shares reserved under the 2011 Plan increased or will increase by the lesser of 1,500,000 shares, 4.0% of the outstanding shares of common stock and common stock equivalents, or another amount determined by the Company's Board of Directors. As of June 30, 2017, 2,205,096 shares of common stock were available for future grant under the 2011 Plan.

Stock-based awards granted to employees generally vest over a three- or four-year period, and, in the case of stock options, expire ten years from the date of grant. Certain awards provide for accelerated vesting if there is a change of control, as defined in the 2005 Plan or 2011 Plan, as applicable. The Company has generally granted stock options at exercise prices not less than the fair market value of its common stock on the date of grant.

## Stock Options

The following summarizes service-based stock option activity under stock incentive plans for the six months ended June 30, 2017:

|                                  | Number<br>of<br>Shares | Weighted-<br>Average<br>Exercise<br>Price<br>per<br>Share | Weighted-<br>Average<br>Remaining<br>Contractual<br>Life<br>(in years) | Aggregate<br>Intrinsic<br>Value<br>(in thousands) (1) |
|----------------------------------|------------------------|---|--|---|
| Outstanding at December 31, 2016 | 1,334,877              | \$ 11.32  |  | \$ 6,787  |
| Granted                          | —                      | —   |  |   |
| Exercised                        | (309,765)              | 10.75   |  |   |
| Forfeited                        | (24,688)               | 12.52   |  |   |
| Outstanding at June 30, 2017     | 1,000,424              | \$ 11.46  | 6.39   | \$ 11,945   |
| Exercisable as of June 30, 2017  | 759,972                | \$ 11.22  | 6.00   | \$ 9,259  |

(1) The aggregate intrinsic value is calculated as the positive difference, if any, between the exercise price of the underlying stock options and the fair market value of the Company's common stock on June 30, 2017.

The Company generally estimates the fair value of stock options on the date of grant using the Black-Scholes option-pricing model. This model requires the use of highly subjective estimates and assumptions, including expected stock price volatility, expected term of an award, risk-free interest rate, and expected dividend yield.

## Restricted Stock Units

The Company recognizes non-cash compensation expense over the vesting term of restricted stock units. The fair value is measured based upon the number of units and the closing price of the Company's common stock underlying such units on the dates of grant. Upon vesting and settlement, each restricted stock unit entitles the holder to receive one share of common stock. The following table summarizes restricted stock unit activity for the six months ended June 30, 2017:

|   | Number of<br>Shares | Weighted Average<br>Grant Date Fair<br>Value |
|---|---------------------|--|
| Unvested restricted stock units as of December 31, 2016 | 1,369,996           | \$ 11.32                                     |
| Restricted stock units granted                          | 640,351             | 19.40  |
| Restricted stock units vested                           | (353,533 )          | 11.07  |

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|   |            |          |
|---|------------|----------|
| Restricted stock units forfeited                    | (139,331 ) | 12.10    |
| Unvested restricted stock units as of June 30, 2017 | 1,517,483  | \$ 14.72 |

17

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Table of Contents

## Restricted Stock Awards

The Company grants restricted stock awards to members of the Board of Directors annually. The fair value is measured based upon the number of units and the closing price of the Company's common stock underlying such units on the dates of grant. Awards to directors vest in full and become unrestricted shares on the earlier of the one year anniversary of the date of grant, or the date of the Company's next annual meeting of stockholders.

The following table summarizes restricted stock award activity for the six months ended June 30, 2017:

|  | Number of<br>Shares | Weighted Average<br>Grant Date Fair<br>Value |
|--|---------------------|--|
| Unvested restricted stock awards as of December 31, 2016 | 114,622             | \$ 9.55                                      |
| Restricted stock awards granted                          | 50,988              | 21.00  |
| Restricted stock awards vested (restriction lapsed)      | (102,788 )          | 9.50   |
| Restricted stock awards forfeited                        | (375 )              | 10.89  |
| Unvested restricted stock awards as of June 30, 2017     | 62,447              | \$ 18.96                                     |

## Equity Awards with Market-Based Vesting Conditions

On February 10, 2017, the Company granted 149,569 restricted stock units with market-based vesting conditions. These restricted stock units contain both performance and service vesting conditions. These awards will meet the performance vesting condition if, within three years from the date of grant, the closing price per share of the Company's common stock is at least \$25.00 per share for 20 consecutive trading days. Upon achievement of the applicable performance vesting condition, the award will be subject to service vesting, with vesting to occur in four equal quarterly installments over the one-year period following the date of achieving the performance-based vesting conditions, subject to the recipient's continued service to the Company through the applicable vesting date.

On February 1, 2016, the Company granted 325,000 restricted stock units with market-based vesting conditions. These restricted stock units contain both performance and service vesting conditions. These awards will meet the performance vesting condition if, within three years from the date of grant, the closing price per share of the Company's common stock is at least \$15.00 per share for 20 consecutive trading days. Upon achievement of the applicable performance vesting condition, the award will be subject to service vesting, with vesting to occur in four equal quarterly installments over the one-year period following the date of achieving the performance-based vesting conditions, subject to the recipient's continued service to the Company through the applicable vesting date. As of June 30, 2017, the market-based vesting conditions have been achieved associated with this grant.

The Company estimated the fair value and derived service period of the restricted stock units with market-based vesting conditions on the date of grant using a Monte-Carlo simulation. The model requires the use of subjective estimates and assumptions, including expected volatility, risk-free interest rate and dividend yield.

The grant-date stock price and assumptions used to estimate the derived service period and fair value of the equity awards with market-based vesting conditions were as follows:

|                         | As of<br>February<br>10,<br>2017 | As of<br>February<br>1,<br>2016 |   |
|-------------------------|----------------------------------|---------------------------------|---|
| Grant-date stock price  | \$ 19.15                         | \$ 8.95                         |   |
| Assumptions             |                                  |                                 |   |
| Risk-free interest rate | 1.47                             | % 1.01                          | % |
| Expected dividend yield | —                                | % —                             | % |
| Expected volatility     | 41.92                            | % 40.00                         | % |

The Company recognizes the stock-based compensation expense on equity awards with market-based vesting conditions in the consolidated statements of operations over the requisite service period. The achievement of certain market-based vesting conditions may result in the acceleration of recognizing stock-based compensation expense

compared to the original valuation. As of June 30, 2017, the Company had achieved certain market-based vesting conditions, which resulted in additional expense.

18

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Table of Contents

The following table summarizes equity awards with market-based vesting conditions activity for the six months ended June 30, 2017:

|  | Options with<br>Market-Based<br>Vesting<br>Conditions<br>(1) | Weighted Average<br>Grant Date Fair<br>Value | Restricted<br>Stock Units<br>with<br>Market-Based<br>Vesting<br>Conditions | Weighted Average<br>Grant Date Fair<br>Value |
|--|--|--|--|--|
| Unvested market-based vesting awards as of December 31, 2016 | 125,000  | \$ 7.65                                      | 367,500  | \$ 6.00                                      |
| Market-based vesting awards granted                          | —  | —  | 149,569  | 13.60  |
| Market-based vesting awards vested                           | —  | —  | (170,000 )   | 5.88   |
| Market-based vesting awards forfeited                        | —  | —  | (22,500 )  | 4.34   |
| Unvested market-based vesting awards as of June 30, 2017     | 125,000  | \$ 7.65                                      | 324,569  | \$ 9.68                                      |

(1) In addition to the unvested market-based vesting options above, there are 125,000 vested market-based vesting options outstanding and exercisable as of June 30, 2017. As of June 30, 2017, these options had an exercise price of \$14.44, a remaining contractual term of 7.43 years, and an intrinsic value of \$0.9 million.

**Stock-based Compensation Expense**

Stock-based compensation is reflected in the consolidated statement of operations as follows (in thousands):

|  | Three Months<br>Ended<br>June 30, |         | Six Months<br>Ended<br>June 30, |         |
|--|-----------------------------------|---------|---------------------------------|---------|
|  | 2017                              | 2016    | 2017                            | 2016    |
| Cost of revenues                       | \$269                             | \$197   | \$500                           | \$411   |
| Research and development               | 405                               | 229     | 714                             | 514     |
| General and administrative             | 1,983                             | 1,454   | 3,940                           | 3,087   |
| Sales and marketing                    | 531                               | 275     | 811                             | 486     |
| Total stock-based compensation expense | \$3,188                           | \$2,155 | \$5,965                         | \$4,498 |

**10. Income Taxes**

The Company's effective income tax rates were (6.7%) and 20.0% for the three months ended June 30, 2017 and 2016, respectively. The Company's effective income tax rates were 109.5% and (12.2%) for the six months ended June 30, 2017 and 2016, respectively. The Company's effective income tax rate is based upon estimated income before provision for income taxes for the year, composition of the income in different countries, and adjustments, if any, in the applicable quarterly periods for potential tax consequences, benefits and/or resolutions of tax audits or other tax contingencies. For the six months ended June 30, 2017, the effective income tax rate varied from the statutory income tax rate principally due to the release of U.S. valuation allowance as a result of the acquisition of Double-Take, and pre-tax book losses in the U.S. and Switzerland that cannot be benefited. The tax benefit recognized during the six months ended June 30, 2017, consists of a tax benefit for a U.S. valuation allowance release that is partially offset by foreign tax expense. The tax provision recognized during the three months ended June 30, 2017, consists primarily of foreign tax expense.

The Company's effective income tax rate in the three months ended June 30, 2017 differed from the three months ended June 30, 2016 primarily due to an increase in pre-tax book losses in the U.S. and Switzerland that cannot be benefited. The Company's effective income tax rate in the six months ended June 30, 2017 differed from the six months ended June 30, 2016 primarily due to the partial release of U.S. valuation allowance due to a net deferred tax liability recorded in the acquisition of Double-Take. The U.S. net deferred tax liability primarily relates to non-tax deductible intangible assets recognized in the financial statements which generate a deferred tax liability. The net deferred tax liability established is estimated to be a source of income to utilize previously unrecognized deferred tax

assets in the U.S. Therefore, the Company has recorded a discrete tax benefit of \$14.6 million in the six months ended June 30, 2017 for the release of U.S. valuation allowance related to the deferred tax liability recorded in purchase accounting. The U.S. maintains a valuation allowance on the overall U.S. net deferred tax asset as it is deemed more likely than not the U.S. net deferred tax asset will not be realized.



Table of Contents

## 11. Commitments and Contingencies

## Operating Leases

The Company leases facilities under leases that expire at varying dates through 2024. Certain of these leases contain renewal options and require the Company to pay operating costs, including property taxes, insurance, and maintenance.

The Company has lease agreements to rent office space in Boston, Massachusetts (corporate headquarters); Salt Lake City, Utah; and Oakville, Canada; as well as various other locations in North America and Europe. The Company has lease agreements to rent data center space in Wakefield, Massachusetts; Phoenix, Arizona; Chandler, Arizona; Bluffdale, Utah; and Ashburn, Virginia. The Company has data center colocation agreements in place with Iron Mountain and Center 7 to rent colocation space at each of their data centers. The terms of several of these leases include escalating rent and free rent periods. Accordingly, the Company recorded a deferred rent liability related to the free rent and escalating rent payments, such that rent is being recognized on a straight-line basis over the terms of the leases. Rent expense was \$2.3 million and \$2.1 million for the three months ended June 30, 2017 and 2016, respectively, and \$4.5 million and \$4.0 million for the six months ended June 30, 2017 and 2016, respectively. At June 30, 2017 and December 31, 2016, \$4.9 million and \$4.6 million, respectively, was included in accrued expenses and other long-term liabilities related to the deferred rent.

In May 2014, the Company entered into a lease agreement for its new corporate headquarters in Boston, Massachusetts. The initial term of the lease expires on December 31, 2024, and the Company has the option to extend the original term of the lease for one successive five-year period. Upon execution of the lease agreement, the Company was required to post a security deposit of \$0.8 million, which the Company maintains as a letter of credit. The Company's landlord can draw against this letter of credit in the event of default by the Company.

Future non-cancellable minimum lease payments under all operating leases as of June 30, 2017, are as follows (in thousands):

| Years Ended December 31, | Office<br>Leases | Data<br>Center<br>Leases<br>(1) | Total    |
|--------------------------|------------------|---------------------------------|----------|
| Remainder of 2017        | \$2,249          | \$1,711                         | \$3,960  |
| 2018                     | 3,489            | 2,197                           | 5,686    |
| 2019                     | 2,461            | 919                             | 3,380    |
| 2020                     | 2,339            | 837                             | 3,176    |
| 2021                     | 2,396            | 849                             | 3,245    |
| Thereafter               | 6,399            | —                               | 6,399    |
| Total                    | \$19,333         | \$6,513                         | \$25,846 |

(1) Certain amounts in the table above relating to colocation leases for the Company's servers include usage based charges in addition to base rent.

## Other Non-cancellable Commitments

As of June 30, 2017, the Company had non-cancellable commitments to vendors primarily consisting of advertising, marketing and broadband services contracts, as follows (in thousands):

| Years Ended December 31, |         |
|--------------------------|---------|
| Remainder of 2017        | \$3,659 |
| 2018                     | 1,469   |
| 2019                     | 549     |
| 2020                     | 199     |
| 2021                     | —       |
| Total                    | \$5,876 |
| Litigation               |         |

On February 27, 2017, Realtime Data LLC (“Realtime Data”) filed a lawsuit against the Company in the U.S. District Court for the Eastern District of Texas, alleging, that the Company’s online backup storage services infringe upon certain patents held by Realtime Data. Realtime has filed several patent suits over the last few years and the asserted patents have gone through various rounds of litigation and inter partes reviews. Realtime Data seeks an award for damages in an unspecified

Table of Contents

amount and an injunction. The Company is not able to assess with certainty the outcome of this lawsuit or the amount or range of potential damages or future payments associated with this lawsuit at this time. The Company intends to defend itself vigorously.

Although results of litigation and claims cannot be predicted with certainty, the Company is not presently involved in any legal proceeding in which the outcome, if determined adversely to the Company, would be expected to have a material adverse effect on our business, operating results, or financial condition. Regardless of the outcome, litigation can have an adverse impact on the Company because of defense and settlement costs, diversion of management resources, and other factors.

12. Retirement Plan

The Company has a 401(k) defined contribution savings plan for its employees who meet certain employment status and age requirements. The plan allows participants to defer a portion of their annual compensation on a pre-tax basis. The Company makes a matching contribution of up to 4% of each employee's wages. For the three months ended June 30, 2017 and 2016, the Company's matching contributions to the plan were \$0.7 million and \$0.5 million, respectively. For the six months ended June 30, 2017 and 2016, the Company's matching contributions to the plan were \$1.2 million and \$0.9 million, respectively.

13. Restructuring

The Company did not record any restructuring charges for the three and six month periods ended June 30, 2017. For the three and six month periods ended June 30, 2016, the Company recorded an immaterial amount and \$0.8 million of restructuring charges, respectively, associated with the reorganization and consolidation of certain operations as well as disposal of certain assets, due to the EVault acquisition.

The Company did not have any amounts accrued related to restructuring charges as of June 30, 2017 or December 31, 2016, respectively.

14. Borrowings and Credit Arrangements

Convertible Senior Notes

On April 4, 2017, the Company issued, in a private offering, \$143.8 million aggregate principal amount of Convertible Notes, which amount includes \$18.8 million aggregate principal amount of Convertible Notes purchased by the initial purchasers pursuant to their over-allotment option. The Convertible Notes accrue interest at 2.50% per year, payable semiannually in arrears on April 1 and October 1 of each year, beginning on October 1, 2017. The Convertible Notes will mature on April 1, 2022, unless earlier repurchased, redeemed or converted.

The conversion rate for the Convertible Notes is initially 38.7034 shares of Company's common stock per \$1,000 principal amount of Convertible Notes, which is equivalent to an initial conversion price of approximately \$25.84 per share of common stock. Prior to January 1, 2022, the Convertible Notes will be convertible by the holders only upon satisfaction of the following conditions and during following periods:

During any calendar quarter commencing after the calendar quarter ending on June 30, 2017 (and only during such calendar quarter), if the last reported sale price of the Company's common stock for at least 20 trading days 1. (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter is greater than or equal to 130% of the conversion price on each applicable trading day;

2. During the five business day period after any five consecutive trading day period (the "Measurement Period") in which the trading price per \$1,000 principal amount of notes for each trading day of the Measurement Period was less than 98% of the product of the last reported sale price of our common stock and the conversion rate on each such trading day;

3. If the Company calls any or all of the notes for redemption at any time prior to the close of business on the second scheduled trading day immediately preceding the redemption date; and

4. Upon the occurrence of certain specified corporate events.

21

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Table of Contents

On or after January 1, 2022 until the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their notes at any time. The Company may satisfy any conversion obligations by paying or delivering, as the case may be, cash, shares of its common stock or a combination of cash and shares of its common stock, at the Company's election in the manner and subject to the terms and conditions provided in the indenture governing the Convertible Notes.

The Company may redeem for cash all or any portion of the Convertible Notes, at its option, on or after April 5, 2020 if the last reported sale price of the Company's common stock has been at least 130% of the conversion price then in effect for at least 20 trading days (whether or not consecutive), during any 30 consecutive trading day period ending on the trading day immediately preceding the date on which the Company provides notice of redemption at a redemption price equal to 100% of the principal amount of the Convertible Notes to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date. As of June 30, 2017, the Convertible Notes were not redeemable.

The Company received \$138.7 million in proceeds from the issuance of the Convertible Notes, net of debt issuance costs and the discounts to the initial purchasers. The Company used \$39.2 million of the proceeds to repay all amounts outstanding under its revolving credit facility, including the related letters of credit, and \$15.0 million of the proceeds to repurchase shares of its common stock from purchasers of Convertible Notes in privately negotiated transactions effected through one or more of the initial purchasers or their affiliates conducted concurrently with the pricing of the Convertible Notes. The remaining proceeds will be used for general corporate purposes, including potential acquisitions.

In accordance with ASC 470-20, Debt With Conversion and Other Options, the Company separated the Convertible Notes into liability and equity components. The carrying amount of the liability component was calculated by measuring the fair value of a similar liability that does not have an associated convertible feature. The carrying amount of the equity component representing the conversion option was determined by deducting the fair value of the liability component from the par value of the Convertible Notes as a whole. The excess of the principal amount of the liability component over its carrying amount ("debt discount") is amortized to interest expense over the term of the Convertible Notes. The equity component is included in the additional paid-in-capital portion of stockholders' equity on the Company's consolidated balance sheet, and is not remeasured as long as it continues to meet the conditions for equity classification.

In addition, the debt issuance costs and debt discount are allocated between the liability and equity components in proportion to the allocation of the proceeds. The issuance costs and discount allocated to the liability component are capitalized as a reduction of the principal amount of the Convertible Notes payable on the Company's balance sheet and amortized, using the effective-interest method, as additional interest expense over the term of the Convertible Notes. The issuance costs and discount allocated to the equity component is recorded as a reduction to additional paid-in capital. The Convertible Notes consisted of the following (in thousands):

|                                  | June 30,<br>2017 |
|----------------------------------|------------------|
| Liability component:             |                  |
| Principal                        | \$143,750        |
| Less: debt issuance costs (788 ) |                  |
| Less: debt discount (34,179 )    |                  |
| Net carrying amount              | \$108,783        |
| Equity component                 | \$31,451         |

For the three month period ending June 30, 2017, the Company incurred total interest expense associated with the Convertible Notes as follows (in thousands):

|   | Three<br>months<br>ended<br>June<br>30,<br>2017 |
|---|---|
| Interest expense related to contractual interest coupon | \$ 859  |
| Interest expense related to accretion of the discount   | 1,465   |
| Interest expense related to debt issuance costs         | 34  |
| Total   | \$ 2,358  |

Table of Contents

As of June 30, 2017, the net carrying value of the Convertible Notes was \$108.8 million, which is net of unamortized debt issuance costs of \$0.8 million. The effective interest rate on the Convertible Notes, including amortization of debt issuance costs and accretion of the discount, is 8.7%. At June 30, 2017, the conversion option value of the Convertible Notes does not exceed their principal amount since the closing market price of the Company's common stock does not exceed the conversion rate. In addition, the Company has the intent and ability to settle the Convertible Notes in cash. Therefore, the Convertible Notes had no impact on the Company's diluted earnings per share.

Credit Facility

The Company and certain of our subsidiaries entered into a credit agreement with Silicon Valley Bank (the "Credit Facility"), which provided a revolving credit financing of up to \$40.0 million, including a \$5.0 million sub-limit for letters of credit.

On April 4, 2017, in connection with the Convertible Notes, the Company utilized \$39.2 million of the net proceeds from the offering to repay all amounts outstanding under its Credit Facility and thereafter terminated the facility.

Table of Contents

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the fiscal year ended December 31, 2016, as filed on March 16, 2017 with the SEC.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or Exchange Act. Forward-looking statements are often identified by the use of words such as, but not limited to, "anticipate," "believe," "can," "continue," "could," "estimate," "expect," "intend," "may," "will," "plan," "project," "seek," "s," "would," and similar expressions or variations intended to identify forward-looking statements. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" included in our Annual Report on Form 10-K filed with the SEC on March 16, 2017. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We are a provider of data protection solutions for businesses and the IT professionals who serve them. Our product suite, including EVault, Inc. ("EVault") and Double-Take Software, Inc. ("Double-Take"), provides a full complement of backup, disaster recovery and high availability solutions for any size business in locations around the world, all supported by a secure global infrastructure.

We derive the majority of our revenue from subscription fees with consistently strong retention rates and a scalable infrastructure to support our growth. The remainder of our revenue is derived from software arrangements, which often contain multiple revenue elements, such as software licenses, hardware, professional services and post-contract customer support. Our customers come from the following primary sources: SMBs who buy our solutions directly from our website, our inside sales team, or from our network of sales channel partners, and consumers who sign up for Carbonite backup solutions on our website in response to our direct marketing campaigns.

On January 31, 2017, we completed the acquisition of all the outstanding capital stock of Double-Take for a purchase price of \$65.9 million, which was comprised of \$59.7 million in cash paid at closing, net of cash acquired, 332,326 shares of our common stock with a fair value of \$5.7 million and the working capital payment of \$0.5 million. We believe the acquisition strengthens our overall leadership position in the data protection market for mid-sized businesses and strengthens our technology portfolio.

We invest in customer acquisition because the market for our solutions is highly competitive. Our sales model is designed to sell large volumes of our solutions to SMBs globally both directly and through our network of sales channel partners which includes distributors, value-added resellers, and managed service providers.

We support our sales network with a marketing approach that leverages our established brand to drive market awareness and demand generation among the broad population of SMBs and consumers. Our marketing efforts are designed to attract prospective customers and enroll them as paying customers, either through immediate sales, free trials or communication of the benefits of our solutions and development of ongoing relationships.

Our operating costs continue to grow as we invest in strategic acquisitions, new customer acquisition, and research and development to grow SMB market share. We expect to continue to devote substantial resources to integration,



global

24

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## Table of Contents

expansion, customer acquisition, and product innovation. In addition, we expect to invest heavily in our operations to support our anticipated growth.

We generally defer revenue over our customers' subscription periods but expense marketing costs as incurred. As a result of these factors, we expect to continue to incur GAAP operating losses on an annual basis for the foreseeable future. For the three months ended June 30, 2017, we generated revenues of \$59.0 million, compared to \$53.4 million for the three months ended June 30, 2016, an increase of 10%. For the six months ended June 30, 2017, we generated revenues of \$116.1 million, compared to \$101.6 million for the six months ended June 30, 2016, an increase of 14%.

### Our Business Model

As the majority of our business is driven by subscription services, we evaluate the profitability of a customer relationship over its lifecycle. We generally incur customer acquisition costs and capital equipment costs in advance of subscriptions while recognizing revenue ratably over the terms of the subscriptions. As a result, a customer relationship may not be profitable or result in positive cash flow at the beginning of the subscription period, even though it may be profitable or result in positive cash flow over the life of the customer relationship. While we offer monthly, annual and multi-year subscription plans, a majority of our customers are currently on annual subscription plans. The annual or multi-year commitments of our customers enhance management's visibility into revenue, and charging customers at the beginning of the subscription period provides working capital.

### Key Business Metrics

Our management regularly reviews a number of financial and operating metrics, including the following key metrics, to evaluate our business. Bookings and adjusted free cash flow are financial data that are not calculated in accordance with GAAP. The presentation on non-GAAP financial information should not be considered in isolation or as a substitute for, or superior to, the financial information prepared and presented in accordance with GAAP. See "Other Financial Data" for a reconciliation to the most comparable financial measures presented in accordance with GAAP

**Bookings.** We calculate bookings as revenue recognized during a particular period plus the change in total deferred revenue, excluding deferred revenue recorded in connection with acquisitions and divestitures, net of foreign exchange during the same period. Our management uses this measure as a proxy for cash receipts. Bookings represent the aggregate dollar value of customer subscriptions and software arrangements, which may include multiple revenue elements, such as software licenses, hardware, professional services and post-contractual support, received by us during a period. We initially record a subscription fee as deferred revenue and then recognize it ratably, on a daily basis, over the life of the subscription period.

**Annual retention rate.** We calculate annual retention rate as the percentage of subscription customers on the last day of the prior year who remain customers on the last day of the current year, or for quarterly presentations, the percentage of customers on the last day of the comparable quarter in the prior year who remain customers on the last day of the current quarter. Our management uses these measures to determine the stability of our customer base and to evaluate the lifetime value of our customer relationships.

**Renewal rate.** We define renewal rate for a period as the percentage of customers who renew annual or multi-year subscriptions that expire during the period presented. Our management uses this measure to monitor trends in customer renewal activity.

**Adjusted free cash flow.** We calculate adjusted free cash flow by subtracting the cash paid for the purchase of property and equipment and adding the payments related to acquisitions, restructuring, litigation and the cash portion of the lease exit charge from net cash provided by operating activities. Our management uses adjusted free cash flow to assess our business performance and evaluate the amount of cash generated by our business.

Subscription renewals may vary during the year based on the date of our customers' original subscriptions. As we recognize subscription revenue ratably over the subscription period, this generally has not resulted in a material seasonal impact on our revenue but may result in material monthly and quarterly variances in one or more of the key business metrics described above.



Table of Contents

## Second Quarter 2017 Results

For the second quarter of 2017, we announced the following GAAP results:

Revenue for three months ended June 30, 2017 was \$59.0 million, an increase of 10% from \$53.4 million for the three months ended June 30, 2016. Revenue for six months ended June 30, 2017 was \$116.1 million, an increase of 14% from \$101.6 million for the six months ended June 30, 2016.

Cash flow from operations for the three months ended June 30, 2017 was \$2.9 million, compared to \$5.1 million for the three months ended June 30, 2016. Cash flow from operations for the six months ended June 30, 2017 was \$10.6 million, compared to (\$1.7) million for the six months ended June 30, 2016.

## Performance Highlights

The following table presents our performance highlights for certain non-GAAP and other key metrics for the three and six months ended June 30, 2017 and 2016:

|                         | Three Months Ended<br>June 30,         |          | Six Months Ended<br>June 30, |           |   |
|-------------------------|--|----------|------------------------------|-----------|---|
|                         | 2017                                   | 2016     | 2017                         | 2016      |   |
|                         | (in thousands, except percentage data) |          |                              |           |   |
| Key metrics (1):        |  |          |                              |           |   |
| Bookings                | \$63,900                               | \$53,693 | \$126,022                    | \$106,008 |   |
| Annual retention rate   | 86                                     | % 86     | % 86                         | % 86      | % |
| Renewal rate            | 85                                     | % 85     | % 85                         | % 84      | % |
| Adjusted free cash flow | \$2,097                                | \$7,258  | \$4,487                      | \$6,725   |   |

(1) See the Key Business Metrics section for the definition of these key metrics, and refer to the Other Financial Data section for the reconciliation of bookings and adjusted free cash flow to the most directly comparable financial measures presented in accordance with GAAP.

The following table presents our bookings by line of business for the periods presented:

|                | Three Months<br>Ended<br>June 30,      |          |             | Six Months Ended<br>June 30, |           |             |
|----------------|--|----------|-------------|------------------------------|-----------|-------------|
|                | 2017                                   | 2016     | Change<br>% | 2017                         | 2016      | Change<br>% |
|                | (in thousands, except percentage data) |          |             |                              |           |             |
| Consumer       | \$20,901                               | \$21,398 | (2 )%       | \$42,948                     | \$44,348  | (3 )%       |
| SMB            | 42,999                                 | 32,295   | 33 %        | 83,074                       | 61,660    | 35 %        |
| Total bookings | \$63,900                               | \$53,693 | 19 %        | \$126,022                    | \$106,008 | 19 %        |

Our bookings increased by \$10.2 million and \$20.0 million for the three and six month periods ended June 30, 2017, respectively, compared to the corresponding periods in 2016, primarily due to the inclusion of bookings from the acquisition of Double-Take which closed during 2017, and increased sales of higher priced SMB solutions. We continue to focus on growing our relationships with active reseller partners, with bookings related to sales of SMB solutions representing 67% of total bookings for the second quarter of 2017, up from 60% in the second quarter of 2016. Our total bookings growth rate for the three and six month periods ended June 30, 2017 was impacted by a decline in our growth rates in consumer bookings. We expect this trend to continue.

Our adjusted free cash flow has decreased by \$5.2 million for the three month period ended June 30, 2017, compared to the corresponding period in 2016, primarily due the increase in purchases related to investments in our datacenters and the timing of payments compared to the corresponding period in 2016.

Our adjusted free cash flow has decreased by \$2.2 million for the six month periods ended June 30, 2017, compared to the corresponding period in 2016, primarily due the capital investments in our datacenters.



## Table of Contents

### Key Components of our Condensed Consolidated Statements of Operations

#### Revenue

We derive our revenue principally from subscription fees related to our service solutions as well as the sale of software arrangements, which often contain multiple revenue elements, such as software licenses, hardware, professional services and post-contract customer support. We initially record a customer subscription fee as deferred revenue and then recognize it as revenue ratably, on a daily basis, over the life of the subscription period.

#### Cost of revenue

Cost of revenue consists primarily of costs associated with our data center operations and customer support centers, including wages and benefits for personnel, depreciation of equipment, amortization of developed technology, rent, utilities and broadband, equipment maintenance, hosting fees, software license fees, and allocated overhead. The expenses related to hosting our services and supporting our customers are related to the number of customers and the complexity of our services and hosting infrastructure. Our cost of storage has decreased over time due to decreases in storage prices and greater efficiency in our data center operations. We have also experienced a downward trend in the cost of storage equipment and broadband service, which we expect will continue in the future. Over the long term, we expect these expenses to increase in absolute dollars, but decrease as a percentage of revenue due to improved efficiencies in supporting customers.

#### Gross profit and gross margin

Historically, our gross margins have expanded due to the introduction of higher priced solutions targeting both SMBs and consumers, a downward trend in the cost of storage equipment and services, and efficiencies of our customer support personnel in supporting our customers. We expect these trends to continue over the long term.

#### Operating expenses

**Research and development.** Research and development expenses consist primarily of wages and benefits for development personnel, third-party outsourcing costs, hosting fees, consulting fees, rent, and depreciation. We focus our research and development efforts on enhancements and ease of use of our solutions. These efforts result in updated versions and new suites of our SMB and consumer solutions, while not changing the underlying technology. The majority of our research and development employees are located in Canada and at our corporate headquarters in the U.S. We expect that research and development expenses will increase in absolute dollars and as a percentage of revenue on an annual basis as we continue to enhance and expand our services.

**General and administrative.** General and administrative expenses consist primarily of wages and benefits for management, finance, accounting, human resources, legal and other administrative personnel, legal and accounting fees, insurance, and other corporate expenses. We expect that general and administrative expenses will increase in absolute dollars on an annual basis so that we can support the anticipated growth of our business. We expect to add personnel and enhance our internal information systems and incur costs related to operating as a public company.

**Sales and marketing.** Sales and marketing expenses consist primarily of wages and benefits for sales and marketing personnel, advertising costs, creative expenses for advertising programs, credit card fees, commissions paid to third-party partners and affiliates, and the cost of providing free trials. We expect that we will continue to commit significant resources to our sales and marketing efforts to grow our business and awareness of our brand and solutions. We expect that sales and marketing expenses will continue to increase in absolute dollars on an annual basis.

**Restructuring charges.** Restructuring charges consist of charges related to the Company's restructuring efforts associated with the reorganization and consolidation of certain operations as well as disposal of certain assets. See Note 13—Restructuring to our condensed consolidated financial statements included in this Quarterly Report for additional information.

#### Critical Accounting Policies

Our financial statements are prepared in accordance with GAAP. The preparation of our financial statements and related disclosures requires us to make estimates, assumptions, and judgments that affect the reported amount of assets, liabilities, revenue, costs and expenses, and related disclosures. We base our estimates and assumptions on historical experience and other factors that we believe to be reasonable under the circumstances, but all such estimates and assumptions are inherently uncertain and unpredictable. We evaluate our estimates and assumptions on an

ongoing basis. Actual results may differ from those estimates and assumptions, and it is possible that other professionals, applying their own judgment to the same facts and

Table of Contents

circumstances, could develop and support alternative estimates and assumptions that would result in material changes to our operating results and financial condition.

We consider the assumptions and estimates associated with revenue recognition, business combinations, goodwill and acquired intangible assets, income taxes and stock-based compensation to be our critical accounting policies and estimates. For further information on our critical and other significant accounting policies, see the notes to the condensed consolidated financial statements appearing elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K, as filed on March 16, 2017 with the SEC.

## Results of Operations

The following table sets forth, for the periods presented, data from our condensed consolidated statements of operations as a percentage of revenue that each line item represents. The period-to-period comparison of financial results is not necessarily indicative of future results. The information contained in the table below should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q.

|   | Three Months Ended June 30, 2017 |         | Six Months Ended June 30, 2016 |         |
|---|----------------------------------|---------|--------------------------------|---------|
|   | 2017                             | 2016    | 2017                           | 2016    |
|   | (% of revenue)                   |         |                                |         |
| Consolidated statements of operations data: |                                  |         |                                |         |
| Revenue                                     | 100.0 %                          | 100.0 % | 100.0 %                        | 100.0 % |
| Cost of revenue                             | 31.0                             | 29.7    | 30.7                           | 30.2    |
| Gross profit                                | 69.0                             | 70.3    | 69.3                           | 69.8    |
| Operating expenses:                         |                                  |         |                                |         |
| Research and development                    | 18.5                             | 15.7    | 18.3                           | 16.8    |
| General and administrative                  | 18.8                             | 19.4    | 20.6                           | 21.5    |
| Sales and marketing                         | 39.6                             | 32.4    | 40.3                           | 33.7    |
| Restructuring charges                       | 0.0                              | 0.1     | 0.0                            | 0.8     |
| Total operating expenses                    | 76.9                             | 67.6    | 79.2                           | 72.8    |
| (Loss) income from operations               | (7.9 )                           | 2.7     | (9.9 )                         | (3.0 )  |
| Interest (expense) income, net              | (3.8 )                           | (0.2 )  | (2.1 )                         | (0.1 )  |
| Other income (expense), net                 | 1.6                              | 0.2     | 1.0                            | —       |
| (Loss) income before income taxes           | (10.1 )                          | 2.7     | (11.0 )                        | (3.1 )  |
| Provision (benefit) for income taxes        | 0.7                              | 0.5     | (12.0 )                        | 0.4     |
| Net (loss) income                           | (10.8 )%                         | 2.2 %   | 1.0 %                          | (3.5 )% |

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

## Revenue

| Three Months Ended June 30, 2017       |      |        | Six Months Ended June 30, 2016 |      |        |
|--|------|--------|--------------------------------|------|--------|
| 2017                                   | 2016 | Change | 2017                           | 2016 | Change |
| (in thousands, except percentage data) |      |        |                                |      |        |

Revenue \$59,034 \$53,435 \$5,599 10.5% \$116,133 \$101,550 \$14,583 14.4%

Revenue increased for the three and six month periods ended June 30, 2017 as compared to the three and six month periods ended June 30, 2016, primarily due to the inclusion of revenue from our recently acquired Double-Take product offerings and increased sales of higher priced SMB solutions.





Table of Contents

## Cost of revenue, gross profit, and gross margin

|                                  | Three Months Ended June 30,            |          |         |         | Six Months Ended June 30, |          |          |         |
|----------------------------------|--|----------|---------|---------|---------------------------|----------|----------|---------|
|                                  | 2017                                   | 2016     | Change  |         | 2017                      | 2016     | Change   |         |
|                                  | (in thousands, except percentage data) |          |         |         |                           |          |          |         |
| Cost of revenue                  | \$18,311                               | \$15,864 | \$2,447 | 15.4 %  | \$35,666                  | \$30,619 | \$5,047  | 16.5 %  |
| Percent of revenue               | 31.0                                   | % 29.7   | %       |         | 30.7                      | % 30.2   | %        |         |
| Components of cost of revenue:   |  |          |         |         |                           |          |          |         |
| Personnel-related costs          | \$6,693                                | \$6,337  | \$356   | 5.6 %   | \$13,596                  | \$12,003 | \$1,593  | 13.3 %  |
| Hosting and depreciation costs   | 5,292                                  | 5,583    | (291 )  | (5.2 )% | 10,538                    | 11,315   | (777 )   | (6.9 )% |
| Amortization, software and other | 6,326                                  | 3,944    | 2,382   | 60.4 %  | 11,532                    | 7,301    | 4,231    | 58.0 %  |
| Total cost of revenue:           | \$18,311                               | \$15,864 | \$2,447 | 15.4 %  | \$35,666                  | \$30,619 | \$5,047  | 16.5 %  |
| Gross profit                     | \$40,723                               | \$37,571 | \$3,152 | 8.4 %   | \$80,467                  | \$70,391 | \$10,076 | 14.3 %  |
| Gross margin                     | 69.0                                   | % 70.3   | %       |         | 69.3                      | % 69.8   | %        |         |

Our gross margin declined slightly for the three and six month periods ended June 30, 2017 as compared to the three and six month periods ended June 30, 2016, primarily related to an increase in the developed technology amortization associated with the Double-Take acquisition which is included in the three and six month periods ended June 30, 2017. The increase in total costs of revenue in the three and six month periods ended June 30, 2017 is due primarily to an increase in developed technology amortization, an increase in personnel-related costs related to additional headcount and the acquisition of Double-Take personnel, an increase in software expenses and support contracts, partially offset by a decrease in hosting and depreciation costs.

## Operating expenses

## Research and development

|   | Three Months Ended June 30,            |         |         |        | Six Months Ended June 30, |          |         |        |
|---|--|---------|---------|--------|---------------------------|----------|---------|--------|
|   | 2017                                   | 2016    | Change  |        | 2017                      | 2016     | Change  |        |
|   | (in thousands, except percentage data) |         |         |        |                           |          |         |        |
| Research and development                | \$10,927                               | \$8,380 | \$2,547 | 30.4 % | \$21,254                  | \$17,116 | \$4,138 | 24.2 % |
| Percent of revenue                      | 18.5                                   | % 15.7  | %       |        | 18.3                      | % 16.8   | %       |        |
| Components of research and development: |  |         |         |        |                           |          |         |        |
| Personnel-related costs                 | \$8,546                                | \$6,623 | \$1,923 | 29.0 % | \$16,508                  | \$12,977 | \$3,531 | 27.2 % |
| Third-party outsourcing costs           | 263                                    | 160     | 103     | 64.4 % | 737                       | 534      | 203     | 38.0 % |
| Hosting, consulting and other           | 2,118                                  | 1,597   | 521     | 32.6 % | 4,009                     | 3,605    | 404     | 11.2 % |
| Total research and development:         | \$10,927                               | \$8,380 | \$2,547 | 30.4 % | \$21,254                  | \$17,116 | \$4,138 | 24.2 % |

Research and development expenses increased for the three and six month periods ended June 30, 2017, as compared to the three and six month periods ended June 30, 2016, primarily as a result of an increase in personnel-related costs associated with additional research and development headcount and the acquisition of Double-Take research and development employees and an increase in consulting and independent contractor expenses.

Table of Contents

## General and administrative

|   | Three Months Ended June 30,            |          |        | Six Months Ended June 30, |          |          |         |        |
|---|--|----------|--------|---------------------------|----------|----------|---------|--------|
|   | 2017                                   | 2016     | Change | 2017                      | 2016     | Change   |         |        |
|   | (in thousands, except percentage data) |          |        |                           |          |          |         |        |
| General and administrative                | \$11,076                               | \$10,389 | \$687  | 6.6 %                     | \$23,946 | \$21,809 | \$2,137 | 9.8 %  |
| Percent of revenue                        | 18.8                                   | % 19.4   | %      |                           | 20.6     | % 21.5   | %       |        |
| Components of general and administrative: |  |          |        |                           |          |          |         |        |
| Personnel-related costs                   | \$6,286                                | \$5,465  | \$821  | 15.0 %                    | \$12,685 | \$10,533 | \$2,152 | 20.4 % |
| Professional fees                         | 2,745                                  | 2,404    | 341    | 14.2 %                    | 7,550    | 7,178    | 372     | 5.2 %  |
| Consulting, taxes and other               | 2,045                                  | 2,520    | (475 ) | (18.8)%                   | 3,711    | 4,098    | (387 )  | (9.4)% |
| Total general and administrative:         | \$11,076                               | \$10,389 | \$687  | 6.6 %                     | \$23,946 | \$21,809 | \$2,137 | 9.8 %  |

General and administrative expenses increased for the three and six month periods ended June 30, 2017 as compared to the three and six month periods ended June 30, 2016, primarily as a result of increased personnel-related costs associated with additional headcount to support our overall growth and an increase in stock-based compensation expense associated with an increased grant pool and accelerated vesting on performance awards, offset by a decrease in transactional tax expense owed to foreign tax authorities.

## Sales and marketing

|  | Three Months Ended June 30,            |          |         | Six Months Ended June 30, |          |          |          |       |
|--|--|----------|---------|---------------------------|----------|----------|----------|-------|
|  | 2017                                   | 2016     | Change  | 2017                      | 2016     | Change   |          |       |
|  | (in thousands, except percentage data) |          |         |                           |          |          |          |       |
| Sales and marketing  | \$23,373                               | \$17,323 | \$6,050 | 34.9%                     | \$46,793 | \$34,205 | \$12,588 | 36.8% |
| Percent of revenue   | 39.6                                   | % 32.4   | %       |                           | 40.3     | % 33.7   | %        |       |
| Components of sales and marketing:                         |  |          |         |                           |          |          |          |       |
| Personnel-related costs                                    | \$10,822                               | \$8,032  | \$2,790 | 34.7%                     | \$21,791 | \$15,657 | \$6,134  | 39.2% |
| Advertising costs  | 4,432                                  | 3,977    | 455     | 11.4%                     | 9,433    | 8,060    | 1,373    | 17.0% |
| Costs of credit card transactions and offering free trials | 1,772                                  | 1,621    | 151     | 9.3 %                     | 3,525    | 3,311    | 214      | 6.5 % |
| Agency fees, consulting and other                          | 6,347                                  | 3,693    | 2,654   | 71.9%                     | 12,044   | 7,177    | 4,867    | 67.8% |
| Total sales and marketing:                                 | \$23,373                               | \$17,323 | \$6,050 | 34.9%                     | \$46,793 | \$34,205 | \$12,588 | 36.8% |

Sales and marketing expenses increased for the three and six month periods ended June 30, 2017 as compared to the three and six month periods ended June 30, 2016, primarily due to increased personnel-related costs associated with additional sales and marketing headcount and the acquisition of Double-Take sales and marketing employees.

Additionally, advertising costs, agency fees, consulting and other costs increased due to an increase in our overall marketing efforts associated with promoting Carbonite's expanded set of offerings to a broader audience, the inclusion of the Double-Take business in our consolidated results and an increase in consulting expenses.

## Restructuring

We did not record any restructuring charges for the three and six month periods ended June 30, 2017. We recorded restructuring charges of \$0.8 million in the first quarter of 2016, primarily related to the reorganization and consolidation of certain operations as well as disposal of certain assets. See Note 13—Restructuring to our condensed consolidated financial statements included in this Quarterly Report for additional information.

Table of Contents

## Income Taxes

We recorded income tax provision of \$0.4 million and \$0.3 million for the three month periods ended June 30, 2017 and June 30, 2016, respectively. Our effective income tax rates were (6.7%) and 20.0% for the three month periods ended June 30, 2017 and June 30, 2016, respectively. We recorded income tax (benefit) provision of (\$14.0) million and \$0.4 million for the six month periods ended June 30, 2017 and June 30, 2016, respectively. Our effective income tax rates were 109.5% and (12.2%) for the six month periods ended June 30, 2017 and June 30, 2016, respectively. Our effective income tax rate varied from the statutory income tax rate principally due to the release of U.S. valuation allowance as a result of the acquisition of Double-Take, and pre-tax book losses in the U.S. and Switzerland that cannot be benefited. Our tax benefit recognized during the six months ended June 30, 2017, consists of a tax benefit for a U.S. valuation allowance release that is partially offset by foreign tax expense. Our tax provision recognized during the three months ended June 30, 2017, primarily consists of foreign tax expense.

Our effective income tax rate in the three months ended June 30, 2017 differed from the three months ended June 30, 2016 primarily due to an increase in pre-tax book losses in the U.S. and Switzerland that cannot be benefited. Our effective income tax rate in the six months ended June 30, 2017 differed from the six months ended June 30, 2016 primarily due to the partial release of U.S. valuation allowance due to a net deferred tax liability recorded in the acquisition of Double-Take. The U.S. net deferred tax liability primarily relates to non-tax deductible intangible assets recognized in the financial statements which generate a deferred tax liability. The net deferred tax liability established is estimated to be a source of income to utilize previously unrecognized deferred tax assets in the U.S. Therefore, we have recorded a discrete tax benefit of \$14.6 million in the six months ended June 30, 2017 for the release of U.S. valuation allowance related to the deferred tax liability recorded in purchase accounting. The U.S. maintains a valuation allowance on the overall U.S. net deferred tax asset as it is deemed more likely than not the U.S. net deferred tax asset will not be realized.

## Other Financial Data

In addition to our results discussed above determined under GAAP, we believe that bookings, annual retention rate, renewal rate, and adjusted free cash flow are useful to investors in evaluating our operating performance. See the Performance Highlights section for the table presenting our performance highlights for the three and six months ended June 30, 2017 and 2016. Management considers these financial and operating metrics critical to understanding our business, reviewing our historical performance, measuring and identifying current and future trends, and for planning purposes. Securities analysts also frequently use bookings and adjusted free cash flow as supplemental measures to evaluate the overall performances of companies.

Bookings and adjusted free cash flow are financial data that are not calculated in accordance with GAAP. The tables below provide reconciliation of bookings and adjusted free cash flow to revenue and cash provided by operating activities, respectively, the most directly comparable financial measures calculated and presented in accordance with GAAP.

Our management uses annual retention rate to determine the stability of our customer base and to evaluate the lifetime value of our customer relationships. As customers' annual and multi-year subscriptions come up for renewal throughout the calendar year based on the dates of their original subscriptions, measuring retention on a trailing 12 month basis at the end of each quarter provides our management with useful and timely information about the stability of our customer base. Management uses renewal rate to monitor trends in customer renewal activity.

Our management uses bookings as a proxy for cash receipts. Bookings represent the aggregate dollar value of customer subscriptions and software arrangements, which may include multiple revenue elements, such as software licenses, hardware, professional services and post-contractual support, received by us during a period. We initially record a subscription fee as deferred revenue and then recognize it ratably, on a daily basis, over the life of the subscription period. Management uses bookings and adjusted free cash flow as measures of our operating performance; for planning purposes, including the preparation of our annual operating budget; to allocate resources to enhance the financial performance of our business; to evaluate the effectiveness of our business strategies; to provide consistency and comparability with past financial performance; to determine capital requirements; to facilitate a comparison of our results with those of other companies; and in communications with our Board of Directors concerning our financial performance. We also use bookings and adjusted free cash flow as factors when determining

management's incentive compensation. Management believes that the use of bookings and adjusted free cash flow provides consistency and comparability with our past financial performance, facilitates period-to-period comparisons of operations, and also facilitates comparisons with other peer companies, many of which use similar non-GAAP financial measures to supplement their GAAP results.

Table of Contents

Although bookings and adjusted free cash flow are frequently used by investors and securities analysts in their evaluations of companies, these metrics have limitations as analytical tools, and you should not consider them in isolation or as substitutes for analysis of our results of operations as reported under GAAP. Some of these limitations are:

- bookings do not reflect our receipt of payment from customers;
- adjusted free cash flow does not reflect our future requirements for contractual commitments to vendors;
- adjusted free cash flow does not reflect the non-cash component of employee compensation or depreciation and amortization of property and equipment; and
- other companies in our industry may calculate bookings or adjusted free cash flow or similarly titled measures differently than we do, limiting their usefulness as comparative measures.

The following tables present reconciliations of our bookings and adjusted free cash flow to revenue and cash provided by operating activities, respectively, the most directly comparable financial measures calculated and presented in accordance with GAAP.

|   | Three Months Ended June 30, |          | Six Months Ended June 30, |           |
|---|-----------------------------|----------|---------------------------|-----------|
|   | 2017                        | 2016     | 2017                      | 2016      |
|   | (in thousands)              |          |                           |           |
| Revenue   | \$59,034                    | \$53,435 | \$116,133                 | \$101,550 |
| Add change in deferred revenue, net of foreign exchange (excluding acquisitions and divestitures) | 4,866                       | 258      | 9,889                     | 4,458     |
| Bookings  | \$63,900                    | \$53,693 | \$126,022                 | \$106,008 |

|   | Three Months Ended June 30, |         | Six Months Ended June 30, |           |
|---|-----------------------------|---------|---------------------------|-----------|
|   | 2017                        | 2016    | 2017                      | 2016      |
|   | (in thousands)              |         |                           |           |
| Cash provided by (used in) operating activities | \$2,872                     | \$5,084 | \$10,568                  | \$(1,673) |
| Subtract capital expenditures                   | (3,471)                     | (885)   | (10,039)                  | (2,809)   |
| Free cash flow                                  | (599)                       | 4,199   | 529                       | (4,482)   |
| Add acquisition-related payments                | 2,659                       | 2,735   | 3,889                     | 9,791     |
| Add restructuring-related payments              | —                           | 239     | —                         | 341       |
| Add cash portion of lease exit charge           | —                           | 85      | —                         | 151       |
| Add litigation-related payments                 | 37                          | —       | 69                        | 924       |
| Adjusted free cash flow                         | \$2,097                     | \$7,258 | \$4,487                   | \$6,725   |

**Liquidity and Capital Resources**

As of June 30, 2017, we had cash and cash equivalents and marketable securities of \$125.1 million, of which \$110.8 million was held in the United States and \$14.3 million of which was held by our international subsidiaries. If the undistributed earnings of our foreign subsidiaries are needed for our operations in the United States, we would be required to accrue and pay U.S. taxes upon repatriation. Our current plans are not expected to require repatriation of cash and investments to fund our U.S. operations and, as a result, we intend to indefinitely reinvest our foreign earnings to fund our foreign subsidiaries.

**Sources of funds**

We believe, based on our current operating plan, that our existing cash and cash equivalents, marketable securities and cash provided by operations, will be sufficient to meet our anticipated cash needs for at least the next 12 months.

From time to time, we may explore additional financing sources to develop or enhance our solutions, fund expansion, respond to competitive pressures, acquire or to invest in complementary products, businesses or technologies, or to lower our cost of capital, which could include equity, equity-linked, and debt financing. There can be no assurance that any additional financing will be available to us on acceptable terms, if at all. If we raise additional funds through the issuance of equity or convertible debt or other equity-linked securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock.

Table of Contents

On April 4, 2017, we issued, in a private offering, \$143.8 million aggregate principal amount of convertible senior notes (the “Convertible Notes”), which amount includes \$18.8 million aggregate principal amount of Convertible Notes purchased by the initial purchasers pursuant to their over-allotment option. The Convertible Notes accrue interest at 2.50% per year, payable semiannually in arrears on April 1 and October 1 of each year, beginning on October 1, 2017. The Convertible Notes will mature on April 1, 2022, unless earlier repurchased, redeemed or converted.

## Uses of funds

We have increased our operating and capital expenditures in connection with the growth in our operations and the increase in our personnel, and we anticipate that we will continue to increase such expenditures in the future. Our future capital requirements may vary materially from those now planned and will depend on many factors, including:

- potential future acquisition opportunities;
- the levels of advertising and promotion required to acquire and retain customers;
  - expansion of our data center infrastructure necessary to support our growth;
- growth of our operations in the U.S. and worldwide;
- our development and introduction of new solutions; and
- the expansion of our sales, customer support, research and development, and marketing organizations.

Future capital expenditures will focus on acquiring additional data storage and hosting capacity and general corporate infrastructure. We are not currently party to any purchase contracts related to future capital expenditures, other than short-term purchase orders.

## Cash flows

The following table summarizes our net cash inflows (outflows) for the six months ended June 30, 2017 and 2016.

|   | Six Months Ended |            |
|---|------------------|------------|
|   | June 30,         |            |
|   | 2017             | 2016       |
|   | (in thousands)   |            |
| Net cash provided by (used in) operating activities | \$10,568         | \$(1,673 ) |
| Net cash used in investing activities               | \$(71,445 )      | \$(14,910) |
| Net cash provided by (used in) financing activities | \$125,961        | \$(4,245 ) |

## Operating activities

Our cash flows from operating activities are significantly influenced by the amount of our net income (loss), growth in sales and customer growth, changes in working capital accounts, the timing of prepayments and payments to vendors, add-backs of non-cash expense items such as depreciation and amortization, and stock-based compensation expense. In the six months ended June 30, 2017, cash provided by operating activities was \$10.6 million, which was driven by our net income of \$1.2 million, an increase in deferred revenue of \$9.5 million and a net adjustment for non-cash charges of \$1.8 million, primarily comprised of \$10.4 million of depreciation and amortization, \$6.0 million of stock-based compensation expense, \$1.5 million of interest expense related to the non-cash interest expense related to the amortization of debt discount, offset by a gain on disposal of equipment of \$0.9 million, benefit for deferred income taxes of \$15.0 million and other non-cash items of \$0.2 million. These cash inflows were partially offset by an increase in working capital of \$1.9 million.

In the six months ended June 30, 2016, cash used in operating activities was \$1.7 million, which was driven by an increase in working capital of \$15.8 million due primarily to timing of payments and customer receipts, our net loss of \$3.5 million and a decrease in other assets and liabilities of \$0.5 million. These cash outflows were partially offset by a \$4.5 million increase in deferred revenue and a net adjustment for non-cash charges of \$13.6 million, primarily comprised of \$8.4 million of depreciation and amortization, \$4.5 million of stock-based compensation expense, \$0.5 million loss on disposal of equipment and \$0.2 million in other non-cash items.





Table of Contents

## Investing activities

In the six months ended June 30, 2017, cash used in investing activities was \$71.4 million, which was primarily driven by our payment of \$60.2 million in connection with the acquisition of Double-Take, capital expenditures of \$10.0 million, a purchase of marketable securities and derivatives of \$2.4 million, partially offset by proceeds from sale of property and equipment of \$0.5 million, proceeds from maturities of marketable securities of \$0.4 million and proceeds from the sale of businesses of \$0.3 million.

In the six months ended June 30, 2016, cash used in investing activities was \$14.9 million, which was primarily driven by our payment of \$11.6 million in connection with the acquisition of EVault, a purchase of marketable securities and derivatives of \$1.5 million, and capital expenditures of \$2.8 million, offset by proceeds from maturities of marketable securities of \$1.0 million.

## Financing activities

In the six months ended June 30, 2017, cash provided by financing activities was \$126.0 million, which was primarily driven by \$177.8 million proceeds from long-term borrowings, net of debt issuance costs and \$3.3 million proceeds from the exercise of stock options, partially offset by \$39.2 million payments on long-term borrowings and \$15.9 million repurchase of common stock.

In the six months ended June 30, 2016, cash used in financing activities was \$4.2 million, which was primarily driven by a \$4.6 million repurchase of common stock, partially offset by net proceeds from the exercise of stock options of \$0.4 million.

## Off-balance sheet arrangements

As of June 30, 2017, we did not have any off-balance sheet arrangements.

## Contractual obligations

The following table summarizes our contractual obligations at June 30, 2017 (in thousands):

|                                      | Payment Due by Period (1) |                  |           |           |                   |
|--------------------------------------|---------------------------|------------------|-----------|-----------|-------------------|
|                                      | Total                     | Less Than 1 Year | 1-3 Years | 3-5 Years | More Than 5 Years |
|                                      | (in thousands)            |                  |           |           |                   |
| Office lease obligations             | \$19,333                  | \$2,249          | \$5,950   | \$4,735   | \$6,399           |
| Data center lease obligations        | 6,513                     | 1,711            | 3,116     | 1,686     | —                 |
| Convertible notes principal          | 143,750                   | —                | —         | 143,750   | —                 |
| Convertible notes interest           | 17,929                    | 3,554            | 7,188     | 7,187     | —                 |
| Hosted software solution obligations | 2,474                     | 851              | 1,604     | 19        | —                 |
| Consulting obligations               | 1,339                     | 1,339            | —         | —         | —                 |
| Other purchase commitments           | 2,063                     | 1,469            | 414       | 180       | —                 |
| Total                                | \$193,401                 | \$11,173         | \$18,272  | \$157,557 | \$6,399           |

(1) The future payments related to uncertain tax positions have not been presented in the table above due to the uncertainty of the amounts and timing of cash settlement with the taxing authorities. There have been no material changes to our uncertain tax positions in the second quarter of 2017.

(2) Certain amounts in the table above relating to colocation leases for the Company's servers include usage based charges in addition to base rent.

The commitments under our office lease obligations shown above consist primarily of lease payments for our Boston, Massachusetts corporate headquarters, our administrative offices in Salt Lake City, Utah and our research and development facility in Oakville, Ontario, Canada.

Commitments under our data center lease obligations included above consist of Wakefield, Massachusetts; Chandler, Arizona; Phoenix, Arizona; Bluffdale, Utah; and Ashburn, Virginia data centers. Additional commitments within this line consist of data center colocation agreements in place with Iron Mountain and Center 7.

Other purchase commitments shown above consist of contractual commitments to various vendors primarily for advertising, marketing, and broadband services.

Table of Contents

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Quantitative and Qualitative Disclosures about Market Risk

For quantitative and qualitative disclosures about market risk affecting us, see Item 7A “Quantitative and Qualitative Disclosures about Market Risk” in our Annual Report on Form 10-K filed with the SEC on March 16, 2017. Our exposure to market risks has not changed materially from that set forth in our Annual Report.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

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

Changes in Internal Control over Financial Reporting

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

Inherent Limitations on Effectiveness of Controls

Our management, including our Chief Executive Officer and Chief Financial Officer, believes that our disclosure controls and procedures and internal control over financial reporting are designed to provide reasonable assurance of achieving their objectives and are effective at the reasonable assurance level. However, our management does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the controls. The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

See Note 11 – Commitments and Contingencies to our condensed consolidated financial statements included in this Quarterly Report for information concerning litigation. In addition to the Realtime Data lawsuit, from time to time, we have been and may become involved in legal proceedings arising in the ordinary course of our business. Although the results of litigation and claims cannot be predicted with certainty, we are not presently involved in any other legal proceeding in which the outcome, if determined adversely to us, would be expected to have a material adverse effect on our business, operating results, or financial condition. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors.

ITEM 1A. RISK FACTORS

The Company's operations and financial results are subject to various risks and uncertainties that could adversely affect our business, financial condition, liquidity and results of operations. In connection with the offering of convertible notes, the Company disclosed to potential investors the following risks related to such convertible notes: The conditional conversion feature of the convertible notes, if triggered, may materially and adversely affect our financial condition and operating results.

In the event the conditional conversion feature of the convertible notes is triggered, holders of convertible notes will be entitled to convert the convertible notes at any time during specified periods at their option. If one or more holders elect to convert their convertible notes, unless we elect to satisfy our conversion obligation by delivering solely shares of our common stock (other than paying cash in lieu of delivering any fractional share), we would be required to settle a portion or all of our conversion obligation through the payment of cash, which could adversely affect our liquidity. In addition, even if holders do not elect to convert their convertible notes, we could be required under applicable accounting rules to reclassify all or a portion of the outstanding principal of the convertible notes as a current rather than long-term liability, which would result in a material reduction of our net working capital.

The accounting method for convertible debt securities that may be settled in cash, such as the convertible notes, could have a material effect on our reported financial results.

Under Accounting Standards Codification 470-20, Debt with Conversion and Other Options, which we refer to as ASC 470-20, an entity must separately account for the liability and equity components of certain convertible debt instruments (such as the convertible notes) that may be settled entirely or partially in cash upon conversion in a manner that reflects the issuer's economic interest cost. The effect of ASC 470-20 on the accounting for the convertible notes is that the equity component is required to be included in the additional paid-in capital section of stockholders' equity on our consolidated balance sheet, and the value of the equity component would be treated as original issue discount for purposes of accounting for the debt component of the convertible notes. As a result, we will be required to record a greater amount of non-cash interest expense in current periods presented as a result of the amortization of the discounted carrying value of the notes to their face amount over the term of the convertible notes. We will report lower net income (or greater net loss) in our financial results because ASC 470-20 requires interest to include both the current period's amortization of the debt discount and the instrument's coupon interest, which could adversely affect our reported or future financial results, the market price of our common stock and the trading price of the convertible notes.

In addition, under certain circumstances, convertible debt instruments (such as the convertible notes) that may be settled entirely or partly in cash are currently accounted for utilizing the treasury stock method if we have the ability and intent to settle in cash, the effect of which is that the shares issuable upon conversion of the convertible notes are not included in the calculation of diluted earnings per share except to the extent that the conversion value of the convertible notes exceeds their principal amount. Under the treasury stock method, for diluted earnings per share purposes, the transaction is accounted for as if the number of shares of common stock that would be necessary to settle such excess, if we elected to settle such excess in shares, are issued. We cannot be sure that we will be able to

demonstrate and continue to demonstrate the ability or intent to settle in cash or that the accounting standards in the future will continue to permit the use of the treasury stock method. If we are unable to use the treasury stock method in accounting for the shares issuable upon conversion of the convertible notes, then our diluted earnings per share would be adversely affected.

Table of Contents

There have otherwise been no material changes to the risks and uncertainties previously presented in "Item 1A. Risk Factors", in our Annual Report on Form 10-K filed with the SEC on March 16, 2017.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## (a) Sale of Unregistered Securities

Not applicable.

## (b) Use of Proceeds

Not applicable.

## (c) Issuer Purchases of Equity Securities

The following table is a summary of the Company's repurchases of our common stock in the second quarter of 2017:

| Period                         | (a) Total<br>Number of<br>Shares<br>Purchased<br>(1) | (b)<br>Average<br>Price<br>Paid per<br>Share (2) | (c) Total<br>Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | (d) Maximum<br>Number (or<br>Approximate<br>Dollar Value)<br>of Shares that<br>May be<br>Purchased<br>Under the<br>Plans or<br>Programs (3) |
|--------------------------------|--|--|--|---|
| April 1, 2017 - April 30, 2017 | —  | \$ —   | —  | \$ 5,214,409  |
| May 1, 2017 - May 31, 2017     | 11,762   | \$ 21.70   | —  | \$ 5,214,409  |
| June 1, 2017 - June 30, 2017   | 11,762   | \$ 19.50   | —  | \$ 5,214,409  |
|                                | 23,524   |  | —  |   |

(1) During the three months ended June 30, 2017, 23,524 shares were withheld by the Company to satisfy tax withholding obligations in connection with the vesting of restricted stock units.

The average price per share for each of the months in the fiscal quarter was calculated by dividing (a) the sum for the aggregate value of the tax withholding obligations and the aggregate amount paid for shares acquired under the

(2) Company's share repurchase program, described in Note 8—Stockholders' Equity to its condensed consolidated financial statements, by (b) the sum of the number of shares withheld and the number of shares acquired in the Company's share repurchase program.

In May 2015, the Company's Board of Directors authorized a \$20.0 million share repurchase program, announced (3) on May 14, 2015 and effective from May 15, 2015 through May 15, 2018. On March 22, 2017, the Company's Board of Directors authorized an increase of \$10.0 million to the share repurchase program.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable.

## ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

## ITEM 5. OTHER INFORMATION

None.





Table of Contents

ITEM 6. EXHIBITS

Exhibits

- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certifications of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certifications of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS XBRL Instance Document.
- 101.SCH XBRL Taxonomy Extension Schema Document.
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document.
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document.
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document.
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.

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.

CARBONITE, INC.

Dated: August 7, 2017 By: /s/ Anthony Folger  
Anthony Folger  
Chief Financial Officer

Dated: August 7, 2017 By: /s/ Cassandra Hudson  
Cassandra Hudson  
Chief Accounting Officer