

MITEK SYSTEMS INC

Form 10-Q

February 08, 2019

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

Form 10-Q

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

For the quarterly period ended December 31, 2018

**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 001-35231

MITEK SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware 87-0418827

(State or Other (I.R.S. Employer
Jurisdiction of Identification
No.)

Incorporation or
Organization)

600 B
Street, Suite
100 92101
San Diego,
California

(Address of
Principal
Executive
Offices) (Zip Code)

(619) 269-6800

(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

(Do not
check if a

Non-accelerated filer

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 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

There were 38,734,691 shares of the registrant's common stock outstanding as of January 31, 2019.

MITEK SYSTEMS, INC.
FORM 10-Q
For The Quarterly Period Ended December 31, 2018
INDEX

PART I
FINANCIAL
INFORMATION

<u>Item 1.</u>	<u>Financial</u>	<u>1</u>
	<u>Statements</u>	
	<u>Consolidated</u>	
	<u>Balance Sheets at</u>	
	<u>December 31, 2018</u>	<u>1</u>
	<u>(Unaudited) and</u>	
	<u>September 30, 2018</u>	
	<u>Consolidated</u>	
	<u>Statements of</u>	
	<u>Operations and</u>	
	<u>Other</u>	
	<u>Comprehensive</u>	
	<u>Loss (Unaudited)</u>	<u>2</u>
	<u>for the Three</u>	
	<u>Months Ended</u>	
	<u>December 31, 2018</u>	
	<u>and 2017</u>	
	<u>Consolidated</u>	
	<u>Statements of</u>	
	<u>Stockholders' Equity</u>	
	<u>(Unaudited) for the</u>	<u>3</u>
	<u>Three Months</u>	
	<u>Ended December</u>	
	<u>31, 2018 and 2017</u>	
	<u>Consolidated</u>	
	<u>Statements of Cash</u>	
	<u>Flows (Unaudited)</u>	
	<u>for the Three</u>	<u>4</u>
	<u>Months Ended</u>	
	<u>December 31, 2018</u>	
	<u>and 2017</u>	
	<u>Notes to</u>	
	<u>Consolidated</u>	
	<u>Financial</u>	<u>5</u>
	<u>Statements</u>	
	<u>(Unaudited)</u>	
<u>Item 2.</u>	<u>Management's</u>	<u>26</u>
	<u>Discussion and</u>	
	<u>Analysis of</u>	

Financial Condition
and Results of
Operations

<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>32</u>
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<u>Item 4.</u>	<u>Controls and Procedures</u>	<u>33</u>
----------------	------------------------------------	-----------

**PART II. OTHER
INFORMATION**

<u>Item 1.</u>	<u>Legal Proceedings</u>	<u>34</u>
----------------	--------------------------	-----------

<u>Item 1A.</u>	<u>Risk Factors</u>	<u>34</u>
-----------------	---------------------	-----------

<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>34</u>
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<u>Item 3.</u>	<u>Defaults Upon Senior Securities</u>	<u>34</u>
----------------	--	-----------

<u>Item 4.</u>	<u>Mine Safety Disclosures</u>	<u>34</u>
----------------	------------------------------------	-----------

<u>Item 5.</u>	<u>Other Information</u>	<u>34</u>
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<u>Item 6.</u>	<u>Exhibits</u>	<u>35</u>
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	<u>Signatures</u>	<u>37</u>
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PART I
FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS.
MITEK SYSTEMS, INC.
CONSOLIDATED BALANCE SHEETS
(amounts in thousands except share data)

	December 31, 2018 (Unaudited)	September 30, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 10,437	\$ 9,028
Short-term investments	9,248	8,448
Accounts receivable, net	12,831	16,821
Prepaid expenses	2,096	2,278
Other current assets	2,455	1,053
Total current assets	37,067	37,628
Property and equipment, net	4,779	4,665
Intangible assets, net	30,742	32,947
Goodwill	34,058	34,407
Deferred income tax assets	16,716	15,356
Other non-current assets	2,815	2,147
Total assets	\$ 126,177	\$ 127,150
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 4,507	3,573
Accrued payroll and related taxes	6,202	7,915
Deferred revenue, current portion	4,655	4,792
Acquisition-related contingent consideration	1,823	1,849
Other current liabilities	2,023	2,278
Total current liabilities	19,210	20,407

Deferred revenue, non-current portion	407	485
Deferred income tax liabilities	8,055	8,162
Other non-current liabilities	2,937	2,702
Total liabilities	30,609	31,756
Stockholders' equity:		
Preferred stock, \$0.001 par value, 1,000,000 shares authorized, none issued and outstanding	—	—
Common stock, \$0.001 par value, 60,000,000 shares authorized, 38,638,816 and 37,961,224 issued and outstanding, as of December 31, 2018 and September 30, 2018, respectively	39	38
Additional paid-in capital	120,199	116,944
Accumulated other comprehensive loss	(1,397)	(586)
Accumulated deficit	(23,273)	(21,002)
Total stockholders' equity	95,568	95,394
Total liabilities and stockholders' equity	\$ 126,177	\$ 127,150

See accompanying notes to consolidated financial statements.

MITEK SYSTEMS, INC.**CONSOLIDATED STATEMENTS OF OPERATIONS AND OTHER COMPREHENSIVE LOSS****(Unaudited)**

(amounts in thousands except per share data)

	Three Months Ended December 31,	
	2018	2017
Revenue		
Software and hardware	\$ 9,995	\$ 7,206
Service and other	7,688	4,930
Total revenue	17,683	12,136
Operating costs and expenses		
Cost of revenue—software and hardware	845	719
Cost of revenue—service and other	2,033	898
Selling and marketing	7,208	4,775
Research and development	4,488	3,280
General and administrative	5,842	3,517
Acquisition-related costs and expenses	1,827	1,259
Total operating costs and expenses	22,243	14,448
Operating loss	(4,560)	(2,312)
Other income, net	14	190
Loss before income taxes	(4,546)	(2,122)
Income tax benefit (provision)	1,355	(3,614)
Net loss	\$ (3,191)	(5,736)
Net loss per share—basic and diluted	\$ (0.08)	\$ (0.17)
Shares used in calculating net loss per share—basic and diluted	38,247	34,207

Other
comprehensive loss

Net loss	\$	(3,191)	(5,736)
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Foreign currency
translation
adjustment

(824)	189
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Unrealized gain
(loss) on
investments

13	(59)
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Other

comprehensive loss	\$	(4,002)	(5,606)
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See accompanying notes to consolidated financial statements.

2

MITEK SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited)
(amounts in thousands except per share)

Three Months Ended December 31, 2018							
	Common Stock Outstanding Shares	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity	
Balance, September 30, 2018	37,96	\$ 38	\$ 116,944	\$ (21,002)	\$ (586)	\$ 95,394	
Exercise of stock options	135	—	586	—	—	586	
Settlement of restricted stock units	543	1	(1)	—	—	—	
Stock-based compensation expense	—	—	2,670	—	—	2,670	
Cumulative-effect adjustment from the adoption of ASU 2014-09	—	—	—	920	—	920	
Components of other comprehensive loss:							
Net loss	—	—	—	(3,191)	—	(3,191)	
Currency translation adjustment	—	—	—	—	(824)	(824)	
Change in unrealized gain on investments	—	—	—	—	13	13	
Total other comprehensive loss						(4,002)	
Balance, December 31, 2018	38,63	\$ 39	\$ 120,199	\$ (23,273)	\$ (1,397)	\$ 95,568	

Three Months Ended December 31, 2017							
	Common Stock Outstanding Shares	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity	
Balance, September 30, 2017	33,72	\$ 34	\$ 78,677	\$ (17,450)	\$ 147	\$ 61,408	
Exercise of stock options	63	—	137	—	—	137	
Settlement of restricted stock units	450	—	—	—	—	—	

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Acquisition-related shares issued	666	1		5,607					5,608		
Stock-based compensation expense	—	—		1,889	—		—		1,889		
Amortization of closing shares	—	—		710	—		—		710		
Cumulative-effect adjustment from the adoption of ASU 2016-09	—	—		—	8,255		—		8,255		
Components of other comprehensive loss:											
Net loss	—	—		—	(5,736)		—		(5,736)		
Currency translation adjustment	—	—		—	—		189		189		
Change in unrealized loss on investments	—	—		—	—		(59)		(59)		
Total other comprehensive loss									(5,606)		
Balance, December 31, 2017	34,90	\$	35	\$	87,020	\$	(14,931)	\$	277	\$	72,401

See accompanying notes to consolidated financial statements..

MITEK SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(amounts in thousands)

	Three Months Ended December 31,	
	2018	2017
Operating activities:		
Net loss	\$ (3,191)	\$ (5,736)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Stock-based compensation expense	2,670	1,889
Amortization of closing and earnout — shares		355
Amortization of intangible assets	1,774	484
Depreciation and amortization	373	91
Amortization of investment premiums and other	(9)	(46)
Deferred taxes	(1,631)	4,417
Changes in assets and liabilities:		
Accounts receivable	3,925	3,065
Other assets	(733)	(1,549)
Accounts payable	943	307
Accrued payroll and related taxes	(1,809)	(1,389)
Deferred revenue	(205)	(326)
Other liabilities	189	1,005
Net cash provided by operating activities	2,296	2,567
Investing activities:		

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Purchases of investments	(1,728)	(15,391)
Sales and maturities of investments	950	9,950
Acquisitions, net of cash acquired	—	(2,991)
Purchases of property and equipment	(508)	(216)
Net cash used in investing activities	(1,286)	(8,648)
Financing activities:		
Proceeds from the issuance of equity plan common stock	586	137
Principal payments on other borrowings	(164)	—
Net cash provided by financing activities	422	137
Foreign currency effect on cash and cash equivalents	(23)	(4)
Net increase (decrease) in cash and cash equivalents	1,409	(5,948)
Cash and cash equivalents at beginning of period	9,028	12,289
Cash and cash equivalents at end of period	\$ 10,437	\$ 6,341
Supplemental disclosures of cash flow information:		
Cash paid for income taxes	\$ 69	\$ 9
Supplemental disclosures of non-cash investing and financing activities:		
	\$ 13	\$ (59)

Unrealized holding
gain (loss) on
available-for-sale
investments

See accompanying notes to consolidated financial statements....

4

MITEK SYSTEMS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Mitek Systems, Inc. ("Mitek" or the "Company") is a leading innovator of mobile capture and digital identity verification solutions. Mitek is a software development company with expertise in artificial intelligence and machine learning. The Company is currently serving more than 6,100 financial services organizations and leading marketplace and financial technology ("fintech") brands across the globe. The Company's solutions are embedded in native mobile apps and mobile optimized websites to facilitate better mobile user experiences, fraud detection and reduction, and compliant transactions.

Mitek's Mobile Deposit® solution is used today by millions of consumers in the United States ("U.S."), Canada, the United Kingdom, and Australia for mobile check deposit. Mobile Deposit® is the category leading product that allows individuals and businesses to remotely deposit checks using their camera-equipped smartphone or tablet. The Company's Mobile Deposit® solution has now processed over two billion check deposits. Mitek began selling Mobile Deposit® in the second fiscal quarter of 2008, and received our first patent issued for this product in August 2010. Mitek's Mobile Verify™ is an important technology used to verify people's identities at the point of onboarding via web or mobile device. Scanning an identity document enables an enterprise to identify the person with whom they are conducting business, comply with growing governmental Know Your Customer and Anti-Money Laundering regulatory requirements, and to improve the overall customer experience for digital onboarding. To sure the person submitting the identity document is who they say they are, Mitek's Mobile Verify Face Comparison provides an incremental layer of verification and compares the face on the identity document with the selfie photo of the user. Mitek's Mobile Verify Face Comparison technology uses advanced liveness detection so it cannot be spoofed. The identification capture process provided by Mitek can also provide prefill of much of the data obtained from the identity document into an application, requiring far fewer key strokes, reducing keying errors, and improving both operational efficiency and the customer experience. Today, the financial services verticals (banks, credit unions, lenders, payments processors, card issuers, fintech companies, etc.) represent the greatest percentage of use of the Company's solutions, but marketplaces, sharing economy, telecommunications, healthcare, travel, and retail sectors are showing accelerated adoption. Similarly, websites that must verify the customer's age (or other consumer information) prior to selling goods can do so by verifying identity documents. Mitek uses machine learning to constantly improve the product performance of Mobile Verify™ and applies artificial intelligence to increase automation and speed of approvals of identification documents.

The core of the Company's user experience is Mitek MiSnap™, a touch-free automated capture technology which can be incorporated across product lines. It provides a simple and superior user-experience, making transactions on mobile devices fast, accurate, and easy for the consumer while helping organizations drive revenue from the increasingly popular mobile channel.

Mobile Fill™, Mitek's mobile identity capture solution, enables the camera to serve as a keyboard. Using Mobile Fill™, consumers can quickly prefill any form with personal data by simply snapping a picture of their driver's license, credit card, or other similar identity document.

CheckReader™, which the Company acquired through the acquisition of A2iA (as defined below), enables financial institutions to automatically extract data from a check image received across all deposit channels – branch, ATM, Remote Deposit Capture, and mobile. Through the automatic recognition of all fields on checks, whether handwritten or machine print, CheckReader™ speeds the time to deposit for banks and customers and reduces costs formerly incurred before images could be exchanged.

ID_CLOUD™ is a fully automated identity verification solution that can be integrated into a customers' application to instantly read and validate identity documents. ID_CLOUD™ automated technology enables global enterprises to improve their customer acquisition technology while meeting AML requirements in a safe and cost-effective manner. This solution is available in the cloud, via mobile websites, and desktop applications. Additionally, a version of ID_CLOUD™ is available that works locally on a desktop which is connected to a propriety hardware scanner for reading and validating identity documents. ID_CLOUD™ is a fully automated identity verification solution that can be

integrated into a customers' application to instantly read and validate identity documents. ID_CLOUD™ automated technology enables global enterprises to improve their customer acquisition technology while meeting AML requirements in a safe and cost-effective manner. This solution is available in the cloud, via mobile websites, and desktop applications. Additionally, a version of ID_CLOUD™ is available that works locally on a desktop which is connected to a propriety hardware scanner for reading and validating identity documents.

5

The Company markets and sells its products and services worldwide through internal, direct sales teams located in the U.S., Europe, and Latin America as well as through channel partners. The Company's partner sales strategy includes channel partners who are financial services technology providers and identity verification providers. These partners integrate the Company's products into their solutions to meet the needs of their customers.

As of December 31, 2018, the Company has been granted 49 patents and it has an additional 21 patent applications pending.

Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated financial statements of the Company as of December 31, 2018 have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and, accordingly, they do not include all information and footnote disclosures required by accounting principles generally accepted in the U.S. ("GAAP"). The Company believes the footnotes and other disclosures made in the financial statements are adequate for a fair presentation of the results of the interim periods presented. The financial statements include all adjustments (solely of a normal recurring nature) which are, in the opinion of management, necessary to make the information presented not misleading. You should read these financial statements and the accompanying notes in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2018, filed with the U.S. Securities and Exchange Commission on December 14, 2018.

Results for the three months ended December 31, 2018 are not necessarily indicative of results for any other interim period or for a full fiscal year.

Principles of Consolidation

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

Foreign Currency

The Company has foreign subsidiaries that operate and sell products and services in various countries and jurisdictions around the world. As a result, the Company is exposed to foreign currency exchange risks. For those subsidiaries whose functional currency is not the U.S. dollar, assets and liabilities are translated into U.S. dollars at the exchange rate in effect on the balance sheet date and revenues and expenses are translated into U.S. dollars using the average exchange rate over the period. Resulting currency translation adjustments are recorded in accumulated other comprehensive loss in the consolidated balance sheets. The Company recorded a net loss resulting from foreign exchange translation of \$0.8 million for the three months ended December 31, 2018 and a net gain resulting from foreign exchange translation of \$0.2 million for the three months ended December 31, 2017.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, deferred taxes, and related disclosure of contingent assets and liabilities. On an ongoing basis, management reviews its estimates based upon currently available information. Actual results could differ materially from those estimates. These estimates include, but are not limited to, assessing the collectability of accounts receivable, estimation of the value of stock-based compensation awards, fair value of assets and liabilities acquired, impairment of goodwill, useful lives of intangible assets, standalone selling price related to revenue recognition, contingent consideration, and income taxes.

Revenue Recognition

The Company recognizes revenue in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 606, *Revenue from Contracts with Customers*, and its related amendments (collectively known as "ASC 606"). ASC 606 outlines a single comprehensive model to use in accounting for revenue arising from contracts with customers. The core principle, involving a five-step process, of the revenue model is that an entity recognizes revenue 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.

The Company generates revenue primarily from the delivery of licenses (to both on premise and transactional software as a service ("SaaS") products) and related services, as well as the delivery of hardware and professional services. Revenue is measured based on consideration specified in a contract with a customer. The Company

recognizes revenue when it satisfies a

6

performance obligation by transferring control over a product or service to a customer which may be at a point in time or over time. See Note 2 of the consolidated financial statements for additional details.

Net Loss Per Share

The Company calculates net loss per share in accordance with FASB ASC Topic 260, *Earnings per Share*. Basic net loss per share is based on the weighted-average number of common shares outstanding during the period. Diluted net loss per share also gives effect to all potentially dilutive securities outstanding during the period, such as restricted stock units (“RSUs”), stock options, and Employee Stock Purchase Plan (“ESPP”) shares, if dilutive. In a period with a net loss position, potentially dilutive securities are not included in the computation of diluted net loss because to do so would be antidilutive, and the number of shares used to calculate basic and diluted net loss is the same.

For the three months ended December 31, 2018 and 2017, the following potentially dilutive common shares were excluded from the calculation of net loss per share, as they would have been antidilutive (*amounts in thousands*):

	Three Months Ended December 31,	
	2018	2017
Stock options	3,033	3,062
RSUs	2,949	2,786
ESPP common stock equivalents	70	—
Total potentially dilutive common shares outstanding	6,052	5,848

The calculation of basic and diluted net loss per share is as follows (*amounts in thousands, except per share data*):

	Three Months Ended December 31,	
	2018	2017
Net loss	\$ (3,191)	\$ (5,736)
Weighted-average shares outstanding—basic	38,247	34,207
Common stock equivalents	—	—
Weighted-average shares outstanding—diluted	38,247	34,207
Net loss per share:		
Basic	\$ (0.08)	\$ (0.17)
Diluted	\$ (0.08)	\$ (0.17)

Investments

Investments consist of corporate notes and bonds, commercial paper, and U.S. Treasury securities. The Company classifies investments as available-for-sale at the time of purchase and reevaluates such classification as of each

balance sheet date. All investments are recorded at estimated fair value. Unrealized gains and losses for available-for-sale securities are included in accumulated other comprehensive loss, a component of stockholders' equity. The Company evaluates its investments to assess whether those with unrealized loss positions are other-than-temporarily impaired. Impairments are considered to be other-than-temporary if they are related to deterioration in credit risk or if it is likely that the Company will sell the securities before the recovery of its cost basis. Realized gains and losses and declines in value judged to be other-than-temporary are determined based on the specific identification method and are reported in other income, net in the consolidated statements of operations and other comprehensive loss. No other-than-temporary impairment charges were recognized in the three months ended December 31, 2018 and 2017.

All investments whose maturity or sale is expected within one year are classified as "current" on the consolidated balance sheets. All other securities are classified as "long-term" on the consolidated balance sheets.

Accounts Receivable and Allowance for Doubtful Accounts

Trade accounts receivable are recorded at the net invoice value and are not interest bearing. The Company considers receivables past due based on the contractual payment terms. Allowances for doubtful accounts are established based on various factors, including credit profiles of the Company's customers, contractual terms and conditions, historical payments, and current economic trends. The Company reviews its allowances by assessing individual accounts receivable over a specific aging and amount. Accounts receivable are written off on a case-by-case basis, net of any amounts that may be collected. The Company had no write-offs of the allowance for doubtful accounts for the three months ended December 31, 2018 and 2017.

The Company maintained an allowance for doubtful accounts of \$0.4 million and \$0.3 million as of December 31, 2018 and September 30, 2018, respectively.

Capitalized Software Development Costs

Costs incurred for the development of software that will be sold, leased, or otherwise marketed are capitalized when technological feasibility has been established. Software development costs consist primarily of compensation of development personnel and related overhead incurred to develop new products and upgrade and enhance the Company's current products, as well as fees paid to outside consultants. Capitalization of software development costs ceases, and amortization of capitalized software development costs commences when the products are available for general release. For the three months ended December 31, 2018 and 2017, no software development costs were capitalized because the time period and costs incurred between technological feasibility and general release for all software product releases were not material or were not realizable. We had no amortization expense from capitalized software costs during the three months ended December 31, 2018 and 2017.

Costs related to software acquired, developed, or modified solely to meet our internal requirements, with no substantive plans to market such software at the time of development, are capitalized. Costs incurred during the preliminary planning and evaluation stage of the project and during post implementation operational stage are expensed as incurred. Costs incurred during the application development stage of the project are capitalized. The Company defines the design, configuration, and coding process as the application development stage. The Company capitalized \$49,000 and \$54,000 of costs related to computer software developed for internal use during the three months ended December 31, 2018 and 2017, respectively. The Company had \$81,000 in amortization expense from internal use software during the three months ended December 31, 2018 and no amortization expense from internal use software during the three months ended December 31, 2017.

Goodwill and Purchased Intangible Assets

The Company's goodwill and intangible assets resulted from prior acquisitions. Goodwill and intangible assets with indefinite useful lives are not amortized, but are tested for impairment at least annually or as circumstances indicate that their value may no longer be recoverable. In accordance with ASC Topic 350, *Intangibles—Goodwill and Other*, the Company reviews its goodwill and indefinite-lived intangible assets for impairment at least annually in its fiscal fourth quarter and more frequently if events or changes in circumstances occur that indicate a potential reduction in the fair value of its reporting unit and/or its indefinite-lived intangible asset below their respective carrying values. Examples of such events or circumstances include: a significant adverse change in legal factors or in the business climate, a significant decline in the Company's stock price, a significant decline in the Company's projected revenue or cash flows, an adverse action or assessment by a regulator, unanticipated competition, a loss of key personnel, or the presence of other indicators that would indicate a reduction in the fair value of a reporting unit. No such events or circumstances have occurred since the last impairment assessment was performed.

The Company's goodwill is considered to be impaired if management determines that the carrying value of the reporting unit to which the goodwill has been assigned exceeds management's estimate of its fair value. Based on the guidance provided by ASC 350 and ASC Topic 280, *Segment Reporting*, management has determined that the Company operates in one segment and consists of one reporting unit given the similarities in economic characteristics between its operations and the common nature of its products, services and customers. Because the Company has only one reporting unit, and because the Company is publicly traded, the Company determines the fair value of the reporting unit based on its market capitalization as it believes this represents the best evidence of fair value. In the fourth quarter of fiscal 2018, management completed its annual goodwill impairment test and concluded that the Company's goodwill was not impaired. The Company's conclusion that goodwill was not impaired was based on a comparison of its net assets to its market capitalization.

Because the Company determines the fair value of its reporting unit based on its market capitalization, the Company's future reviews of goodwill for impairment may be impacted by changes in the price of the Company's common stock, par value \$0.001 per share ("Common Stock"). For example, a significant decline in the price of the Common Stock may cause the fair value of its goodwill to fall below its carrying value. Therefore, the Company cannot assure that when it completes its future reviews of goodwill for impairment a material impairment charge will not be recorded. Intangible assets are amortized over their useful lives. Each period, the Company evaluates the estimated remaining useful life of its intangible assets and whether events or changes in circumstances warrant a revision to the remaining

period of amortization. The carrying amounts of these assets are periodically reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of these assets may not be recoverable. Recoverability of these assets is measured by comparing the carrying amount of each asset to the future undiscounted cash flows the asset is expected to generate. The carrying amount of such assets is reduced to fair value if the undiscounted cash flows used in the test for recoverability are less than the carrying amount of such assets.

8

Income Taxes

The Company accounts for income taxes in accordance with FASB ASC Topic 740, *Income Taxes*. Deferred tax assets and liabilities arise from temporary differences between the tax bases of assets and liabilities and their reported amounts in the financial statements that will result in taxable or deductible amounts in future years.

Management evaluates the available evidence about future taxable income and other possible sources of realization of deferred tax assets. The valuation allowance reduces deferred tax assets to an amount that represents management's best estimate of the amount of such deferred tax assets that more likely than not will be realized. See Note 7 of the consolidated financial statements for additional details.

The Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the tax authorities, based on the technical merits of the position. The tax benefit is measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The Company recognizes interest and penalties related to income tax matters in income tax expense. See Note 7 of the consolidated financial statements for additional details.

Stock-Based Compensation

The Company issues RSUs, stock options, performance options, and Senior Executive Long Term Incentive Restricted Stock Units ("Senior Executive Performance RSUs") as awards to its employees. Additionally, eligible employees may participate in the Company's ESPP. Employee stock awards are measured at fair value on the date of grant and expense is recognized using the straight-line single-option method in accordance with FASB ASC Topic 718, *Compensation-Stock Compensation*. Forfeitures are recorded as they occur.

The Company assigns fair value to RSUs based on the closing stock price on the date of grant.

The Company estimates the fair value of stock options and ESPP shares using the Black-Scholes option pricing model. The Black-Scholes option pricing model requires subjective assumptions, including future stock price volatility and expected time to exercise, which greatly affect the calculated values. The expected term of options granted is derived from historical data on employee exercises and post-vesting employment termination behavior. The risk-free rate selected to value any particular grant is based on the U.S. Treasury rate that corresponds to the expected life of the grant effective as of the date of the grant. The expected volatility is based on the historical volatility of the Company's stock price. These factors could change in the future, affecting the determination of stock-based compensation expense in future periods.

The Company estimates the fair value of Senior Executive Performance RSUs, performance options, and similar awards using the Monte-Carlo simulation. The Monte-Carlo simulation requires subjective assumptions, including the Company's valuation date stock price, the annual risk-free interest rate, expected volatility, the probability of reaching the performance targets, and a 20-trading-day average stock price.

Other Borrowings

The Company has certain loan agreements with Spanish government agencies which were assumed when the Company acquired ICAR Vision Systems, S.L. ("ICAR"). These agreements have repayment periods of five to twelve years and bear no interest. As of December 31, 2018, \$0.6 million was outstanding under these agreements and \$0.2 million and \$0.4 million is recorded in other current liabilities and other non-current liabilities, respectively, in the consolidated balance sheets. As of September 30, 2018, \$0.8 million was outstanding under these agreements and \$0.3 million and \$0.5 million was recorded in other current liabilities and other non-current liabilities, respectively, in the consolidated balance sheets.

Guarantees

In the ordinary course of business, the Company is not subject to potential obligations under guarantees that fall within the scope of FASB ASC Topic 460, *Guarantees* ("ASC 460"), except for standard indemnification and warranty provisions that are contained within many of the Company's customer license and service agreements and certain supplier agreements, and give rise only to the disclosure requirements prescribed by ASC 460. Indemnification and warranty provisions contained within the Company's customer license and service agreements and certain supplier agreements are generally consistent with those prevalent in the Company's industry. The Company has not historically incurred significant obligations under customer indemnification or warranty provisions and does not expect to incur significant obligations in the future. Accordingly, the Company does not maintain accruals for potential customer indemnification or warranty-related obligations.

Comprehensive Loss

Comprehensive loss consists of net loss, unrealized gains and losses on available-for-sale securities, and foreign currency translation adjustments. Included on the consolidated balance sheets is accumulated other comprehensive loss of \$1.4 million and \$0.6 million at December 31, 2018 and September 30, 2018, respectively.

9

Recently Adopted Accounting Pronouncements

In October 2016, the FASB issued Accounting Standards Update (“ASU”) No. 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory* (“ASU 2016-16”), which eliminates the current prohibition on immediate recognition of the current and deferred income tax effects of intra-entity transfers of assets other than inventory, with the intent of reducing complexity and diversity in practice. Under ASU 2016-16, entities must recognize the income tax consequences when the transfer occurs rather than deferring recognition. For public entities, ASU 2016-16 is effective for fiscal years, including interim periods within those fiscal years, beginning after December 15, 2017. Entities must apply