Crexendo, Inc.
Form 10-K
March 04, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2013:

Or

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

Crexendo, Inc.
(Exact name of registrant as specified in its charter)

Delaware	001-32277	87-0591719
(State or Other Jurisdiction of Incorporation or Organization)	(Commission File Number)	(I.R.S. Employer Identification No.)

1615 South 52nd Street, Tempe, AZ 85281
(Address of Principal Executive Office) (Zip Code)

(602) 714-8500
(Registrant's telephone number, including area code)
(Former name, former address and former fiscal year, if changed since last report)

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

Title of each class	Name of each exchange on which registered
Common Stock, par value $0.001 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

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

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

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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, 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 þ No o

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

Large accelerated filer o   Accelerated filer o   Non-accelerated filer o   Smaller reporting company þ

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

The aggregate market value of the common stock held by non-affiliates of the registrant as of December 31, 2013 was approximately $16,514,000.

The number of shares of the registrant's common stock outstanding as of March 1, 2014 was 10,827,926.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Registrant's 2014 Annual Meeting of Stockholders are incorporated by reference in Part III of this Annual Report on Form 10-K.

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PART I

Throughout this Annual Report, we refer to Crexendo, Inc., together with its subsidiaries, as “we,” “us,” “our Company” or “the Company.” As used in this Annual Report, “StoresOnline™” and “Ride The Cloud” are registered trademarks of our Company in the United States and other countries. All other product names are or may be trademarks of, and are used to identify the products and services of, their respective owners.

THIS ANNUAL REPORT ON FORM 10-K CONTAINS FORWARD-LOOKING STATEMENTS. THESE STATEMENTS RELATE TO FUTURE EVENTS OR OUR FUTURE FINANCIAL PERFORMANCE. IN SOME CASES, YOU CAN IDENTIFY FORWARD-LOOKING STATEMENTS BY TERMINOLOGY SUCH AS “MAY,” “WILL,” “SHOULD,” “EXPECT,” “PLAN,” “INTEND,” “ANTICIPATE,” “BELIEVE,” “ESTIMATE,” “PROJECT,” “PRE “POTENTIAL” OR “CONTINUE” (INCLUDING THE NEGATIVE OF SUCH TERMS), OR OTHER SIMILAR TERMINOLOGY. THESE STATEMENTS ARE ONLY ESTIMATIONS, AND ARE BASED UPON VARIOUS ASSUMPTIONS THAT MAY NOT BE REALIZED. ACTUAL EVENTS OR RESULTS MAY DIFFER MATERIALLY. IN EVALUATING THESE STATEMENTS, YOU SHOULD SPECIFICALLY CONSIDER VARIOUS FACTORS, INCLUDING, BUT NOT LIMITED TO, THE RISKS OUTLINED BELOW UNDER ITEM 1A. THESE FACTORS MAY CAUSE OUR ACTUAL RESULTS TO DIFFER MATERIALLY FROM ANY FORWARD-LOOKING STATEMENT.

ALTHOUGH WE BELIEVE THAT THE ESTIMATIONS REFLECTED IN THE FORWARD-LOOKING STATEMENTS ARE REASONABLE, WE CANNOT GUARANTEE FUTURE RESULTS, LEVELS OF ACTIVITY, PERFORMANCE OR ACHIEVEMENTS. MOREOVER, NEITHER WE NOR ANY OTHER PERSON ASSUMES RESPONSIBILITY FOR THE ACCURACY AND COMPLETENESS OF THE FORWARD-LOOKING STATEMENTS. WE DO NOT INTEND TO UPDATE ANY OF THE FORWARD-LOOKING STATEMENTS AFTER THE DATE OF THIS ANNUAL REPORT TO CONFORM SUCH STATEMENTS TO ACTUAL RESULTS OR TO CHANGES IN OUR EXPECTATIONS, UNLESS REQUIRED BY LAW.

ITEM 1. BUSINESS

OVERVIEW

We are a hosted services company that provides website hosting, hosted telecommunications services, e-commerce software, website development software, and broadband internet services for businesses and entrepreneurs. Our services are designed to make enterprise-class hosting services available to small and medium-sized businesses at affordable monthly rates. The Company has three operating segments, which consist of Crexendo Network Services, Crexendo Web Services, and StoresOnline.

Crexendo Network Services segment - Our hosted telecommunications services transmit calls using IP or cloud technology, which converts voice signals into digital data packets for transmission over the Internet or cloud. Each of our calling plans provides a number of basic features typically offered by traditional telephone service providers, plus a wide range of enhanced features that we believe offer an attractive value proposition to our customers. This platform enables a user, via a single “identity” or telephone number, to access and utilize services and features regardless of how the user is connected to the Internet or cloud, whether it’s from a desktop device or a mobile device.

Crexendo Web Services segment –We generate professional services revenue primarily from search engine optimization services, link building, paid search management services, conversion rate optimization services, and website design and development. These services are typically billed on a fixed price basis or on a monthly recurring basis with an initial term of six to twelve months. During the quarter ended September 30, 2013, the Company made a strategic decision to limit our provision of web services to our enterprise sized customers.

StoresOnline segment – Our StoresOnline segment serves the small office/ home office (SOHO) business owner and entrepreneur seeking the tools and training to establish a successful website on the Internet. Specifically, StoresOnline services a market segment looking for a “do-it-yourself” option as an alternative to the high cost of contracting an e-commerce or lead generation web developer and, most importantly, an ad agency for website promotion. Both are difficult barriers to many entrepreneurs looking to establish a presence on the Internet.

We have historically sold our StoresOnline products and services through a direct mail seminar format utilizing direct response marketing campaigns. In July 2011, we suspended the sale of our products and services through the direct mail seminar format. Following the suspension of the direct mail seminar format, our primary marketing channel for our StoresOnline segment has been through in-house telemarketing, online marketing channels, and direct prospecting.

We generate revenue from the cash collections from our extended payment term agreements (EPTAs), website hosting, and Avail 24/7 services.

We generate subscription fees from our hosted telecommunications and broadband Internet services. Our hosted telecommunications contracts typically have a thirty-six to sixty month term. We generate product revenue and equipment financing revenue from the sale and lease of our hosted telecommunications equipment. Revenues from the sale of equipment, including those from sales-type leases, are recognized at the time of sale or at the inception of the lease, as appropriate.

OUR STRATEGY

We have historically sold our content management and website building tool as a perpetual software license. During 2011, we transitioned from selling a perpetual software license to a “Software as a Service” (“SaaS”) model. This transition provides the foundation for our strategy on a go forward basis. Key elements of our strategy include:

Expanding Our Distribution Channels. To sell hosted telecommunications products and services cost effectively, we must expand our distribution channels. We have historically sold our hosted telecommunications products and services through a direct sales force channel, which relied on experienced sales representatives. During 2013, we began to accelerate plans to expand our distribution channels through direct sales, online marketing, affiliate programs, white-label programs, and dealer channel. These expanded distribution channels will provide multiple revenue streams from customers across a broader spectrum.

Continuing to Target the Entrepreneur and Small and Medium-Sized Business Market Segment. We believe the small and medium-sized business market segment offers us the best opportunity for future growth, but we are capable of handling all sizes of business. We believe this segment needs comprehensive, affordable, and scalable solutions for their telecommunications services. Our services are designed to be scalable to meet the needs of these businesses, regardless of size.

Strengthening Customer Retention. We are dedicated to enhancing customer retention and building lasting relationships with our customers. We believe a critical element in strengthening customer retention is continuous improvement to our content management and web-building tools, including improvements to our user interface to create a more intuitive and interactive experience. We believe staying ahead of the technology curve is a critical element to our customer retention. We are dedicated to developing the features necessary to stay competitive in the hosted telecommunications industry. We are constantly updating and expanding our product and service offerings to meet the needs of our customer base in this dynamic marketplace.

Developing Complimentary Services and Technologies. We seek to develop complimentary products and services for our customers. Our ultimate goal is to become the leading provider of hosted solutions for small and medium-sized business. We currently provide hosted website services, hosted telecommunications services, e-commerce software, website development software, and broadband internet connections.

OUR SERVICES AND PRODUCTS

Our goal is to provide a broad range of cloud-based products and services that nearly eliminate the cost of a businesses’ technology infrastructure and enable businesses of any size to more efficiently run their business. By providing a variety of comprehensive and scalable solutions, we are able to provide these solutions on a monthly basis to businesses and entrepreneurs without the need for expensive capital investments, regardless of where their business is in its lifecycle. Our products and services can be categorized in the following offerings:

Hosted Website Services

Our hosted website services allow businesses and entrepreneurs to host their websites in our data center for a monthly fee.

Hosted Telecommunications Services

Our hosted telecommunications service offering includes hardware and software and unified communication solutions for businesses using IP or cloud technology over any high-speed internet connection. These services are rendered through a variety of devices and user interfaces such as a Crexendo branded desktop phones and mobile and desktop applications. Some examples of mobile devices are Android smart-phones, iPhones, iPads, or Android tablets. These services enable our customers to seamlessly communicate with others through phone calls that originate/terminate on our network or the PSTN network. Our hosted telecommunications services are powered by our proprietary implementation of standard Internet, Web and IP or cloud technologies. Our services also use Crexendo's infrastructure that we build and manage based on industry standard best practices to achieve greater efficiencies and customer satisfaction. Our infrastructure comprises of computing, storage, network technologies, 3rd party products, and vendor relationships. We also develop end user portals for account management, license management, billing and customer support, and adopt other cloud technologies through our partnerships.

Crexendo's hosted telecommunication service offers a wide variety of essential and advanced features and benefits for small and medium-size businesses. Many of these features included in the service offering are:

Business Productivity Features such as dial-by extension and name, transfer, conference, call recording, Unlimited calling to anywhere in US and Canada, International calling, Toll free (Inbound and Outbound)

Individual Productivity Features such as Caller ID, Call Waiting, Last Call Return, Call Recording, Music-On-Hold, Voicemail, Unified Messaging, Hot-Desking

Group Productivity Features such as Call Park, Call Pickup, Interactive Voice Response (IVR), Individual and Universal Paging, Corporate Directory, Multi-Party Conferencing, Group Mailboxes

Call Center Features such as Automated Call Distribution (ACD), Call Monitor, Whisper and Barge, Automatic Call Recording

Advanced Unified Communication Features such as Find-Me-Follow-Me, Sequential Ring and Simultaneous Ring

Mobile Features such as extension dialing, transfer and conference and seamless hand-off from Wifi to/from 3G and 4G, as well as other data services. These features are available on CrexMo, an intelligent mobile application for iPhone and Android smartphones, as well as iPads and Android tablets

Traditional PBX Features such as Busy Lamp Fields, System Hold, 16-48 Port density Analog Devices

Expanded Desktop Device Selection such as Entry Level Phone, Executive Desktop, DECT Phone for roaming users

Advanced Faxing solution such as Cloud Fax (cFax) allowing customers to send and receive Faxes from their Email Clients, Mobile Phones and Desktops without having to use a Fax Machine simply by attaching a file

Web based online portal to Administer, Manage and Provisioning the system, manage the account, billing and activity

Many of these services are available and included in our basic offering to our customers for a monthly recurring fee and do not require a capital expense. Some of the advanced features such as Automatic Call Recording and Call Center Features require additional monthly fees. Crexendo continues to invest and develop its technology and SaaS offering to make it more competitive and profitable.

Search Engine Optimization (SEO)

There are two general aspects to Search Engine Optimization ("SEO"). First, the tactical level, that includes conditioning a website and/or its pages to be relevant and search-engine friendly. Second, we help businesses strategically select keywords and keyword phrases. The popularity of a site plays a role in what keyword phrases a business can compete on versus what keyword phrases might be "out of their league". We focus on the strategic selection of keywords and prioritize keywords that have healthy search volumes and high 'win' capability. Our experience coupled with our software allow us to strategically select the best choices for keyword phrases to target, which provide the highest probability of getting high search engine positions and draws maximum traffic to the website. Our SEO packages include a keyword interview, strategic keyword research, baseline ranking report, search engine optimization plan, and comparison ranking report.

Link Building

Link building is a critical component of off-page SEO. To be effective, a link building campaign must be done manually. Search engines can detect links obtained via automated submission. Also, links need to come from many different types of sites, not just one or two. Link building is closely related to search engine optimization, as such; we carefully synchronize all our link building efforts and anchor text with our search engine optimization efforts.

An effective link building effort is labor intensive, with no real shortcuts. We use a broad based approach for link building that follows search engine webmaster guidelines. We use strategies that include, but aren't limited to: Web 2.0 sites, social media and social bookmarking sites, vertical portals, local directories, live directories, and others.

Paid Search Management

We offer paid search management services, such as management of Google® AdWords™, Yahoo, and Microsoft Advertising adCenter™ accounts for our customers.

Modern paid search networks are incredibly sophisticated and require a tremendous amount of experience and expertise to avoid the many potential pitfalls of paid search. We assist customers by taking a conservative approach to paid search management. By using a combination of proprietary automation tools, split test dedicated landing pages, as well as the practiced eye of an expert monitoring our customer accounts on a daily basis, we are able to consistently raise conversion rates and lower the cost of pay-per-click (PPC) acquisition.

Website Design and Development

Using our proprietary software and processes we design and develop websites with “conversion” in mind. The term conversion means different things to different websites. To a lead-generation website, it means getting prospects to submit their contact information so the sales team can contact them. For an e-commerce website, conversion means getting an online customer to complete an order.

Our website design packages range from a semi-custom template based design package to a completely custom design package. We incorporate analytics into every website we build. Proper analytics allow identification of weak spots in the conversion process. Once weak spots are identified, the site can be adjusted to smooth out the process and help turn more prospects into customers.

Once the site is complete, we provide tutorials and tools to allow customers to make changes to their sites as often as necessary without having to pay additional programming fees. Alternatively, customers can elect to have us manage the changes to their websites for an additional fee.

SEGMENT INFORMATION

The Company has three operating segments, which consist of Crexendo Network Services, Crexendo Web Services, and StoresOnline. Effective October 1, 2012, the Company changed its reporting segments to reflect the allocation of previously unallocated corporate expenses to each of the three operating segments. The Company revised its segment reporting to reflect changes in how the Chief Operating Decision Maker (CODM) internally measures performance and allocates resources. Segment operating results for the prior year have been revised to conform to current year segment operating results presentation. Segment revenue and income (loss) before income tax provision was as follows (in thousands):

	Year Ended December 31,	
	2013	2012
Revenue:		
StoresOnline segment	$5,908	$13,857
Crexendo Web Services segment	2,050	2,505
Crexendo Network Services segment	2,370	805
Consolidated	$10,328	$17,167

	Year Ended December 31,	
	2013	2012
Income (loss) before income tax provision:		
StoresOnline segment	$2,528	$6,487
Crexendo Web Services segment	(2,319)	(5,277)
Crexendo Network Services segment	(5,429)	(5,363)
Loss before income tax provision	$(5,220)	$(4,153)

TECHNOLOGY

We believe our proprietary implementation of standard Web, VoIP, Mobile, and Internet technologies represent a key component of our business model. We believe these technologies and how we deliver them to our customers distinguish our services and products from the services and products offered by our competitors. Our technology infrastructure and virtual network operation center, all of which is built and managed on industry standard computing, storage, data, and platforms offers us greater efficiencies. The synergies between Web and Telecommunication protocols such as TCP/IP, HTTP, XML, SIP, and innovations in computing, load balancing, redundancy and high availability of Web and Telecommunications technologies offers us a unique advantage in delivering these services to our customers seamlessly from our data center.

Our Hosted Telecommunications technology is continuously being enhanced with additional features and functionality. Our current functionality includes:

High-end desktop telephony devices such as Gigabit, PoE, 6 Line Color Phone with 10 programmable buttons, and lower end Monochrome 2 Line wall mountable device.

Basic Business Telephony Features such as those offered in a traditional private branch exchange (“PBX”) systems like extension dialing, Direct Inward Dialing (DID), Hold/Resume, Music-On-Hold, Call Transfer (Attended and Unattended), Conferencing, Local, Long Distance, Toll-Free and International Dialing, Voicemail, Auto-Attendant, and traditional faxing

Advanced telephony features such as Call Park, Call Pickup, Paging(through the phones), Overhead paging, Call Recording

Call Center Functionality such as Agent Log In/Log Out, Whisper, Barge, and Call center reporting

Unified Communications features like Simultaneous Ring, Sequential Ring, Status based Routing (Find-Me-Follow-Me), 10-party instant conference, and Mobile application (CrexMo)

Crexendo Mobile Application (CrexMo), which allows users to place and receive extension calls using Crexendo’s network, transfer and conference other users right from their mobile phone as if they were in the office. It also provides users instant access to visual voicemail and call logs.

End User Portal and Unified Messaging with Voicemail, Call Recording, and eFax inbox.

Our web software platform is continuously being enhanced and is an innovative website-building environment. Features and functions of our software include:

during website development, our customers can experience the look and feel of their websites as if they were their own customers. They can shop, navigate, order products, track orders, and more. If they want to change or add more elements, they can edit, rearrange, add, and delete the elements all within a dynamic, point-and-click environment;

designs that are customized based on the customers’ choices and arrangements. Customers can modify the look and feel of the design to complement their services or products. In addition, design modification and arrangement are executed within a streamlined, point-and-click environment;

blogs, online journals, message boards, and forums that are easily integrated into the content of the website. As administrators, the customers have full control in terms of filtering content, allowing images, and other blog, message board, and forum permissions;

customizable forms that address customer-specific needs. By using customized forms, our customers can set up secure, encrypted forms with improved ease to collect sensitive information from their customers. This is especially useful for service-based businesses, as these forms can be used for job, loan, applications, questionnaires, bids, quotes, lead generation, etc.;

advanced out of the box eCommerce features include: shopping cart, ordering rules setup for shipping, sales tax, discount codes, UPS integration, inventory control system, gift certificate and gift card purchasing and redemption, integration with Amazon® Checkout and/or Google® Checkout, Google® Base integration, eBay® auctions integration, shopping cart supporting multiple currencies and price sets, automatic sitemap generation used by search engines, and advanced website product search using filters to quickly narrow down the product offering based on product attributes.

We continue to invest and develop on our Web platform to make it more easy-to-use, enable larger mobile and 3rd party integration features thus enabling our web customers to drive more traffic to their web-sites.

RESEARCH AND DEVELOPMENT

We invested $1,692,000 and $1,985,000 for the years ended December 31, 2013 and 2012, respectively, in the research and development of our technologies and data center. The majority of these expenditures were for our hosted telecommunications products and services and website development software.

COMPETITION

Our markets are increasingly competitive. Our competitors include hosted telecommunications providers and traditional telephone service providers, application service providers, software vendors, systems integrators, direct providers, and information technology consulting services providers, and hosted service providers.

Most of these competitors, however, do not yet offer the full range of website hosting and telecommunications services we believe our target market requires. These competitors could elect to focus additional resources in our target markets, which could adversely affect our business prospects, financial position and results of operations materially. Many of our current and potential competitors have longer operating histories, larger customer bases, and longer relationships with customers as well as significantly greater financial, technical, marketing and public relations resources than we do.

Additionally, should we determine to pursue acquisition opportunities, we may compete with other companies with similar growth strategies. Some of these competitors may be larger and have greater financial resources than we do. Competition for these acquisition targets could also result in increased prices of acquisition targets and a diminished pool of companies available for acquisition.

There are relatively low barriers to entry into our business. Our proprietary technology does not preclude or inhibit competitors from entering our markets. In particular, we anticipate new entrants will attempt to develop competing products and services or new forums for conducting e-commerce and telecommunications services which could be deemed competition. Additionally, if e-commerce or Internet based enterprises and telecommunications service providers with more resources and name recognition were to enter our markets, they may redefine our industry and make it difficult for us to compete.

Expected technology advances associated with the Cloud, increasing use of the Cloud, and new software products are welcome advancements that we believe will broaden the Cloud’s viability. We anticipate that we can compete successfully by relying on our infrastructure, marketing strategies and techniques, systems and procedures, and by adding additional products and services in the future. We believe we can continue the operation of our business by periodic review and revision to our product offerings and marketing approach.

INTELLECTUAL PROPERTY

Our success depends in part on using and protecting our proprietary technology and other intellectual property. Furthermore, we must conduct our operations without infringing on the proprietary rights of third parties. We also rely upon trade secrets and the know-how and expertise of our key employees. To protect our proprietary technology and other intellectual property, we rely on a combination of the protections provided by applicable copyright, trademark and trade secret laws, as well as confidentiality procedures and licensing arrangements. Although we believe we have taken appropriate steps to protect our intellectual property rights, including requiring employees and third parties who are granted access to our intellectual property to enter into confidentiality agreements, these measures may not be sufficient to protect our rights against third parties. Others may independently develop or otherwise acquire unpatented technologies or products similar or superior to ours.

We license from third parties certain software and Internet tools which we include in our services and products. If any of these licenses were terminated, we could be required to seek licenses for similar software and Internet tools from other third parties or develop these tools internally. We may not be able to obtain such licenses or develop such tools in a timely fashion, on acceptable terms, or at all.

Companies participating in the software, Internet technology, and telecommunication industries are frequently involved in disputes relating to intellectual property. We may be required to defend our intellectual property rights against infringement, duplication, discovery and misappropriation by third parties or to defend against third-party claims of infringement. Likewise, disputes may arise in the future with respect to ownership of technology developed by employees who were previously employed by other companies. Any such litigation or disputes could be costly and divert our attention from our business. An adverse determination could subject us to significant liabilities to third parties, require us to seek licenses from, or pay royalties to, third parties, or require us to develop appropriate alternative technology. Some or all of these licenses may not be available to us on acceptable terms, or at all. In addition, we may be unable to develop alternate technology at an acceptable price, or at all. Any of these events could have a material adverse effect on our business prospects, financial position, or results of operations.

EMPLOYEES

As of December 31, 2013, we had 84 employees; 82 full-time and 2 part-time, including 5 executives, 16 sales representatives, 7 in sales management and administration, 17 engineer and IT support in the development of our cloud services solutions, 15 in Web Services and Network Services fulfillment, 4 in customer support, and 20 in finance, legal and business development, collections, marketing, and other general administration.

CORPORATE INFORMATION

Crexendo, Inc. was incorporated as a Nevada corporation under the name “Netgateway, Inc.” on April 13, 1995. In November 1999, we were reincorporated under the laws of Delaware. In July 2002, we changed our corporate name to “iMergent, Inc.”. In May 2011, our stockholders approved an amendment to our Certificate of Incorporation to change our name from "iMergent, Inc." to "Crexendo, Inc." The name change was effective May 18, 2011. Our ticker symbol "IIG" on the New York Stock Exchange was changed to “EXE” on May 18, 2011. We changed the name to better reflect the scope and direction of our business activities of assisting and providing web-based technology solutions to entrepreneurs and small businesses who are seeking to take advantage of the benefits of conducting business on the cloud.

We are headquartered at 1615 South 52nd Street, Tempe, AZ, 85281, and our telephone number is (602) 714-8500. Our website is www.crexendo.com. Our website and the information contained therein or connected thereto shall not be deemed to be incorporated into this Annual Report.

We make available free of charge on or through our Internet website our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities Exchange and Commission (“SEC”).

You may read and copy this Annual Report at the SEC’s public reference room at 450 Fifth Street, NW, Washington D.C. 20549. Information on the operation of the public reference room can be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements and other information regarding our filings at www.sec.gov.

GOVERNMENTAL REGULATION

We are subject to regulations generally applicable to all businesses. We are also subject to an increasing number of laws and regulations directly applicable to telecom, internet access and commerce. The adoption of any such additional laws or regulations may decrease the rate of growth of the Internet, which could in turn decrease the demand for our products and services. Such laws may also increase our costs of doing business or otherwise have an adverse effect on our business prospects, financial position or results of operations. Moreover, the applicability to the Internet of existing laws governing issues such as property ownership, libel, and personal privacy is uncertain. In particular, one channel we use to initially contact our customers is e-mail. The use of e-mail for this purpose has become the subject of a number of recently adopted and proposed laws and regulations. Future federal or state legislation or regulation could have a material adverse effect on our business prospects, financial condition and results of operations.

ITEM 1A. RISK FACTORS.

In addition to factors discussed elsewhere in this Annual Report, the following are important risks which could adversely affect our future results. If any of the risks we describe below materialize, or if any unforeseen risk develops, our operating results may suffer, our financial condition may deteriorate, the trading price of our common stock may decline and our investors could lose all or part of their investment.

The Company has transformed into a start-up telecom company with the inherent risks and uncertainties of funding operations until profitability is achieved. We currently plan to fund our growth during the next twelve months using our cash and cash equivalents of $3.1 million, the collection of the remaining $545,000 of accounts receivable from our former StoresOnline business, and the $2 million proceeds from the sale of the Crexendo head office to the CEO in the first quarter of 2014 (see Note 16). The Company also received a commitment from the CEO, and major shareholder, in February of 2014 that the CEO would provide the necessary level of financial support to enable the Company to pay its debts as they become due through March 31, 2015. Accordingly the Company believes it will have sufficient funds to sustain its operations during the next 12 months as a result of the sources of funding detailed above.

Changes in laws and regulations and the interpretation and enforcement of such laws and regulations could adversely impact our financial results or ability to conduct business.

We are subject to a variety of federal and state laws and regulations as well as oversight from a variety of governmental agencies and public service commissions. The laws governing our business may change in ways that harm our business. Federal or state governmental agencies administering and enforcing such laws may also choose to interpret and apply them in ways that harm our business. These interpretations are also subject to change. Regulatory action could materially impair or force us to change our business model and may adversely affect our revenue, increase our compliance costs, and reduce our profitability. In addition, governmental agencies such as the Securities and Exchange Commission (SEC), Internal Revenue Service (IRS), Federal Trade Commission (FTC), Federal Communication Commission (FCC) and state taxing authorities may conclude that we have violated federal laws, state laws or other rules and regulations, and we could be subject to fines, penalties or other actions that could adversely impact our financial results or our ability to conduct business.

From time to time we have been the subject of governmental inquiries and investigations related to our discontinued seminar sales model and business practices that could require us pay refunds, damages or fines, which could negatively impact our financial results or ability to conduct business.

From time to time, we received inquiries from federal, national, state, city and local government officials in the various jurisdictions in which we operated. These inquiries had historically been related to our discontinued seminar sales practices. These inquiries and investigations generally concern compliance with various city, county, state, and/or federal regulations involving sales, representations made, customer service, refund policies, and marketing practices. There is still the potential of review of past sales and sales of our current web and telecom services. We respond to these inquiries and have generally been successful in addressing the concerns of these persons and entities, without a formal complaint or charge being made, although there is often no formal closing of the inquiry or investigation. See Part I, Item 3, Legal Proceedings, for a discussion of some of these pending matters. The ultimate resolution of these or other inquiries or investigations may have a material adverse effect on our business or operations, or a formal complaint could be initiated. During the ordinary course of business we also receive a number of complaints and inquiries from customers, governmental and private entities. In some cases these complaints and inquiries have ended up in civil court. While we attempt to resolve these matters on a mutually satisfactory basis, there can be no assurance that the ultimate resolution of these matters will not have a material adverse effect on our business or results of operations. We are also subject to various claims and legal proceedings covering matters which arise in the ordinary course of business. We believe the resolution of these other cases will not have a material adverse effect on our business, financial position, or results of operations.

Our Telecommunications services are required to comply with industry standards, FCC regulations as well as certain State and local jurisdiction specific regulations which may require us to modify existing products and/or services.

The acceptance of telephony services and network services are dependent upon our meeting certain industry standards. Our VoIP telephony products are not currently sold to work with other competitors' or vendors' equipment. There is currently a lack of agreement among industry leaders about whether there should be an industry standard or a preferred standard. Our inability to operate with competitor's equipment or services may impact our competitiveness. We do comply with certain rules and regulations of the FCC regarding safety standards. Standards are continuously being modified and replaced. As standards evolve, we may be required to modify our existing products or develop and support new versions of our products. We must comply with certain federal, state, and local requirements regarding how we interact with our customers, including marketing practices, consumer protection, privacy, and billing issues, the provision of 9-1-1 emergency service and the quality of service we provide to our customers. The failure of our products and services to comply, or delays in compliance, with various existing and evolving standards could delay future offerings and impact our sales, margins, and profitability.

Changes to Universal Service Fund programs could increase the cost of our service to our customers diminishing or eliminating our pricing advantage.

The FCC and a number of states are considering reform or other modifications to Universal Service Fund programs. The way we calculate our contribution may therefore change. The changes if not able to be passed on to our customers could substantially reduce our revenues, margins, and profitability.

States are adding regulation for VoIP carriers which could increase our costs and change certain aspects of our service.

Certain states take the position that offerings by VoIP companies are intrastate and therefore subject to state regulation. We have registered as a CLEC in most states however our rates are not regulated in the same manner as traditional telephone service providers. Some states are also requiring that we register as a seller of VoIP services even though we have registered as a CLEC. Some states argue that if the beginning and end points of communications are known, and if some of these communications occur entirely within the boundaries of a state, the state can regulate that offering and may therefore add additional taxes or surcharges or regulate rates in a similar matter to traditional telephone service providers. We believe that the FCC has pre-empted states from regulating VoIP offerings in the same manner as providers of traditional telecommunications services. We cannot predict how this issue will be resolved or its impact on our business at this time.

Our ability to offer services outside the U.S. is subject to different regulations which may be unknown and uncertain.

Regulatory treatment of VoIP telephony outside the United States varies from country to country, and local jurisdictions. Many times the laws are vague, unclear and regulations are not enforced uniformly. We are licensed as a VoIP seller in Canada, and are considering expanding to other countries. We also cannot control if our customers take their devises out of the United States and use them abroad. Our resellers may sell to customers who maintain facilities outside the United States. The failure by us or our customers and resellers to comply with laws and regulations could reduce our revenue and profitability. As we expand to additional Countries there may be additional regulations that we are required to comply with, the failure to comply or properly assess regulations may subject us to penalties, fines and other actions which could materially affect our business.

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From time to time we are and have been the subject of customer complaints and lawsuits relating to our business practices which could require us to pay damages or fines, and could negatively impact our financial results.

Primarily from our discontinued seminar sales practices, we receive complaints and inquiries from both customers and governmental and non-governmental bodies on behalf of customers and, in some cases, these customer complaints have resulted in litigation. Some of these matters are pending. The ultimate resolution of these matters may have a material adverse effect on our financial position or results of operations.

Changes to rates by our competitors and increasing regulatory charges may diminish or eliminate our competitive pricing advantage.

Pricing in the telecommunications industry is very fluid and competitive. Our competitors may reduce their rates which may diminish or eliminate the competitive pricing advantage of our services or otherwise require us to reduce our rates which would affect our margins and revenues. In addition, increased regulation and additional regulatory funding obligations at various levels of government could require us to either increase our prices or absorb the cost or raise our prices which could make us less competitive. Continued rate decreases could require us to lower our rates to remain competitive which could substantially reduce our revenues, margins, and profitability.

We may be required to reduce our prices in order to compete which could negatively impact our profitability.

As competition with our Web Services and Hosted VoIP (Voice over Internet Protocol) services continues to expand, we may be required to respond to additional competition which could require us to engage in price competition. If intense price competition occurs, we may be forced to lower prices, which could result in lower revenue and gross margins.

The telecommunications industry is highly competitive. We face intense competition from traditional telephone companies, wireless companies, cable companies and alternative voice communication providers.

Our Hosted VoIP telecommunication product competes with other VoIP providers. In addition, we also compete with traditional telephone service providers which provide telephone service based on the public switched telephone network. Some of these traditional service providers also provide internet service to their customers. Our VoIP offering is not fully compatible with such customers. Some of these traditional providers have also added VoIP services. There is also competition from cable providers, which have added VoIP services to their existing cable customers. The telecommunications industry is highly competitive. We face intense competition from traditional telephone companies, wireless companies, cable companies, and alternative voice communication providers.

Most traditional wire line and wireless telephone service providers, cable companies, and some VoIP providers are substantially larger and better capitalized than we are and have the advantage of a large existing customer base. Because most of our target customers are already purchasing communications services from one or more of these providers, our success is dependent upon our ability to attract target customers away from their existing providers. Our competitors' financial resources may allow them to offer services at prices below cost or even for free in order to maintain and gain market share or otherwise improve their competitive positions.

The market for our products and services is evolving and our position in that market is uncertain. We may not have the resources to compete with other companies within our industry.

The markets for our products and services are continuing to evolve and are increasingly competitive. Demand and market acceptance for recently introduced and proposed new products and services and sales of such products and services are subject to a high level of uncertainty and risk. Our business may suffer if the market develops in an unexpected manner, develops more slowly than in the past or becomes saturated with competitors, if any new products and services do not sustain market acceptance.

Many of our direct competitors offer a range of products and services comparable to those offered by us. These competitors at any time could elect to focus additional resources in our target markets, which could materially and adversely affect us. Many of our current and potential competitors have stronger brand recognition, longer operating histories, larger customer bases, longer relationships with customers, and significantly greater financial, technical, marketing and public relations resources than we do. We believe our competitors may be able to adapt more quickly to new technologies and customer needs, devote greater resources to the promotion or sale of their products and services, initiate or withstand substantial price competition, take advantage of acquisition or other opportunities more readily or develop and expand their product and service offerings more quickly.

There are low barriers to entry into the e-commerce services and Hosted VoIP telecommunication markets and, as a result, we face significant competition in a rapidly evolving industry.

We currently do not have patented technology, and only a limited amount of other proprietary technology, that would preclude or inhibit competitors from entering our business. Although we have patents pending, we currently do not have any registered patents. In addition, the costs to develop and provide e-commerce and VoIP services are relatively low. Therefore, we expect that we will continually face additional competition from new entrants into the market in the future. There is also the risk that our employees or independent contractors may leave and start competing businesses. The emergence of these enterprises could have a material adverse effect on us. Existing or future competitors may better address new developments or react more favorably to changes within our industry and may develop or offer e-commerce services providing significant technological, creative, performance, price, or other advantages over the services that we offer.

Increased competition, including the entry of new competitors, the introduction of new products by new and existing competitors, or price competition, could have a materially adverse effect on operating results and financial condition.

A number of very large, well-capitalized, high profile companies serve the e-commerce VoIP and technology markets. If any of these companies entered our markets in a focused and concentrated fashion, we could lose customers, particularly more sophisticated and financially stable customers, and our revenue and profitability would suffer. These potential competitors could likely offer a broad array of products and services that would compete favorably with our product offerings. They could also likely offer these products at prices that would be difficult for us to match.

The rates we pay to underlying telecommunications carriers are subject to change and may impact our operations.

Interconnected VoIP traffic may be subject to increased charges. Should this occur, the rates paid to our underlying carriers may increase which could reduce our profitability. Changes in our underlying rates may change rates we charge our customers which could impact our sales and retention of customers as well as make us less competitive.

FCC Regulations regarding payments between regulated carriers may increase our costs.

The FCC adopted changes regarding repayments between regulated carriers that we partner with to interface with the public switch telephone network. The rates we pay for the services performed by these carriers may increase as a result of the FCC's reform order. As a result, we may increase rates for service, making our offerings less competitive with others in the marketplace, or reduce our profitability. The FCC further reformed the system under which regulated providers of telecommunications services compensate each other for various types of traffic, including VoIP traffic that terminates on the PSTN and applied new call signaling requirements to VoIP and other service provider. This may also affect our cost structure and our competitiveness.

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We have incurred operating losses.

We sustained operating losses in the current and prior years. Our ability to obtain positive cash flows from operating activities will depend on many factors including, but not limited to, our ability to (i) reduce costs, (ii) improve sales and marketing efficiencies, (iii) reach more highly qualified prospects, and (iv) achieve operational improvements.

Our new lines of business have not been profitable.

We recorded operating losses on our Crexendo Network Services and Crexendo Web Services segments for the period ending December 31, 2012 and 2013 of $10,670,000 and $7,748,000, respectively. We have incurred operating losses in each of the three prior years and may incur operating losses in the foreseeable future.

If the market for our new products does not develop as we anticipate, our revenue may decline or fail to grow, which would adversely affect our operating results.

We market our Crexendo Web Services and Network Services. The market for these products is still evolving and it is uncertain whether these products and services will achieve and sustain high levels of demand and market acceptance. If potential customers do not perceive the benefits of our product lines, sales may not develop or may develop more slowly than we expect, either of which would adversely affect our operations. Because the market for new product development is difficult to predict, we may make errors in predicting and reacting to relevant business trends, which may have a material adverse effect on our consolidated financial position, results of operations, and cash flows.

Our ability to use our net operating loss carry-forwards may be reduced in the event of an ownership change, and could adversely affect our financial results.

As of December 31, 2013, we had net operating loss (“NOL”) carry-forwards of approximately $13,219,000, of which $5,761,000 is subject to Section 382 limitations. Section 382 of the Internal Revenue Code, as amended (the “Code”) imposes limitations on a corporation’s ability to utilize its NOL carry-forwards. In general terms, an ownership change results from transactions increasing the ownership of certain stockholders in the stock of a corporation by more than 50% over a three-year period. Since our formation, we have issued a significant number of shares, and purchasers of those shares have sold some of them, resulting in two ownership changes, as defined by Code Section 382. As a result of the most recent ownership change, utilization of our NOL is subject to an annual limitation determined by multiplying the value of our stock at the time of the ownership change by the applicable federal long-term tax-exempt rate. The annual limitation is approximately $461,000. Any limited amounts may be carried over into later years, and the amount of the limitation may, under certain circumstances, be increased by the “recognized built-in gains” that occur during the five-year period after the ownership change (the recognition period). Future changes in ownership of more than 50% may also limit the use of these remaining NOL carry-forwards. Our earnings, if any, and cash resources would be materially and adversely affected if we cannot receive the full benefit of the remaining NOL carry-forwards. An ownership change could occur as a result of circumstances that are not within our control.

We are subject to the risk of future disruptive technologies. If new technologies develop that are able to deliver competing voice and messaging services at lower prices, better or more conveniently, it could have a material adverse effect on us.

Our VoIP service competes against established alternative voice communication providers, (such as 8x8 and Ring Central). While we believe the technology we employ provides substantially better quality, changes in technology could allow these alternative providers to deliver comparable quality at a substantially lower price. In addition, as we continue providing VoIP services, we are likely to face competition from emerging competitors focused on newer, less costly technology. In order to compete with such service providers, we may have to reduce our prices, which would impair our profitability, or offer additional features that may cause us to incur additional costs without commensurate price increases.

If we fail to adapt to changes in the market then our products and services could become obsolete.

The market for our products and services is constantly and rapidly evolving. There is substantial competition for our e-commerce services and our Hosted VoIP telecommunications products and services. As competitors introduce new and enhanced products and services, we may not be able to develop or acquire new products and services that compete effectively. New products based on new technologies or new industry standards could render our existing products obsolete and unmarketable. Any technical flaws in products we release could have a negative effect on customer adoption and our reputation.

Fluctuations in our operating results may affect our stock price and ability to raise capital.

Our operating results for any given quarter or fiscal year should not be relied upon as an indication of future performance. Quarter to quarter comparisons of our results of operations may not be meaningful as a result of (i) our limited operating history relating to Crexendo Web Services and Crexendo Network Services and (ii) the emerging nature of the markets in which we compete. Our future results will fluctuate, and those results may fall below the expectations of investors and may cause the trading price of our common stock to fall. This may impair our ability to raise capital, should we seek to do so. Our quarterly results may fluctuate based on, but not limited to, the following factors:

Our ability to attract and retain customers;

FCC or other regulatory charges which we may not be able to “pass on”;

Competition from other telecommunication offerings;

Negative publicity about our industry, events, or products;

Fluctuations in collections of our extended payment term agreements;

Changes in pricing policies;

Regulatory actions and legal proceedings;

Internet and online services usage levels and the rate of market acceptance of these services for transacting commerce;

Our ability to timely and effectively upgrade and develop our systems and infrastructure;

Changes to our business model resulting from regulatory requirements;

Our ability to control certain costs;

Our ability to attract, train and retain skilled management, as well as sales, strategic, technical, and creative professionals;

The availability of working capital and the amount and timing of costs relating to our expansion; and

General economic conditions and economic conditions that are specific to internet technology usage and e-commerce.

Future sales of our common stock by our existing stockholders and stock options granted by us could adversely affect our stock price.

The market price of our common stock could decline as a result of sales of a large number of shares of our common stock in the market or the perception that these sales could occur. These sales also might make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate. As of March 1, 2014, we had outstanding 10,827,926 shares of common stock.

Additional dilution will result if outstanding options to acquire shares of our common stock are exercised. As of March 1, 2014, we had outstanding options to purchase 1,945,766 shares of our common stock. In addition, in the event future financings are required they could be convertible into or exchangeable for our equity securities, investors may experience additional dilution.

Our Chief Executive Officer owns a significant amount of our common stock and could exercise substantial corporate control.

Steven G Mihaylo, our Chief Executive Officer ("CEO"), owns approximately 45% of the outstanding shares of our common stock based on the number of shares outstanding as of March 4, 2014. As a result, Mr. Mihaylo may have the ability to determine the outcome of matters submitted to our stockholders for approval, including the election of directors and any merger, amalgamation, consolidation or sale of all or substantially all of our assets. Mr. Mihaylo may have the ability to control the management and affairs of our Company. As a director and officer, Mr. Mihaylo owes a fiduciary duty to our stockholders. As a stockholder, Mr. Mihaylo is entitled to vote his shares, in his own interests, which may not always be in the interests of our stockholders generally. Accordingly, even though certain transactions may be in the best interests of other stockholders, this concentration of ownership may harm the market price of our common stock by, among other things, delaying, deferring or preventing a change in control of our Company, impeding a merger, amalgamation, consolidation, takeover or other business combination involving our Company, or discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of our Company.

In addition, sales or other dispositions of our shares by Mr. Mihaylo may depress our stock price. Sales of a significant number of shares of our common stock in the public market could harm the market price of our common stock. As additional shares of our common stock become available for resale in the public market, the supply of our common stock will increase, which could result in a decrease in the market price of our common stock.

Lack of sufficient stockholder equity or continued losses from operations could subject us to fail to comply with the listing requirements of NYSE MKT, if that occurred, the price of our common stock and our ability to access the capital markets could be negatively impacted, and our business will be harmed.

Our common stock is currently listed on New York Stock Exchange Market, or NYSE MKT. We have stockholders' equity of $6,701,000 as of December 31, 2013 and we have had annual losses from continuing operations for the last three years with the possibility of continued losses, it is possible we may not remain in compliance with the minimum condition of NYSE MKT's continued listing standards under Section 1003(a) (1) of NYSE MKT's Company Guide (the "Company Guide"). We have not received a formal written notification of non-compliance. In the event of a formal written notification, we believe we would be allowed to respond and attempt to take action to regain compliance with the minimum listing standards. However, in the event we are not able to meet the requirements necessary for continued listing on the NYSE MKT, including those related to minimum stockholder equity requirements, our stock could be subject to delisting from NYSE MKT. Delisting from the NYSE MKT could negatively affect the trading price of our stock and could also have other negative results, including the potential loss of confidence by suppliers and employees, the failure to attract the interest of institutional investors, and fewer business development opportunities. In addition, we would be subject to a number of restrictions regarding the registration and qualification of our common stock under federal and state securities laws. The NYSE MKT could also, in its discretion, discontinue listing our Company’s common stock pursuant to various other factors, including if our independent registered public accountants’ opinion on our financial statements contained a qualified opinion or unqualified opinion with a “going concern” emphasis or the Company is unable to meet current financial obligations or to adequately finance our operations.

Our stock price could decline further because of the activities of short sellers.

The activities of short sellers could further reduce the price of our stock or inhibit increases in our stock price.

Our business could be materially and adversely affected as a result of general economic and market conditions.

We are subject to the effects of general global economic and market conditions. Unfavorable changes in economic conditions, including inflation, recession, or other changes in economic conditions may cause businesses and entrepreneurs to curtail or eliminate spending for our products and services. An adverse change in economic conditions may adversely affect our business.

If we do not successfully expand our sales including our dealer program, direct sales and sales channels, we may be unable to substantially increase our sales.

We sell our products primarily through direct sales, inside sales and our telecommunications dealer program, and we must expand the number of dealers and producing direct sales personnel to increase revenue substantially. If we are unable to expand our dealer network and the sales per dealer and hire and retain qualified sales personnel or if new sales personnel fail to develop the necessary skills to be productive, or if they reach productivity more slowly than anticipated, our ability to increase our revenue and grow our business could be compromised. Our sales personnel may require a long period of time to become productive. The time required in achieving efficiency, as well as the challenge of attracting, training, and retaining qualified candidates, may make it difficult to grow revenue.

Our ability to provide telecommunications services is dependent upon third-party facilities and equipment, the failure of which could cause delays or interruptions of our service and impact our revenue and profitability.

Our ability to provide quality and reliable telephony service is in part dependent upon the proper functioning of facilities and equipment owned and operated by third parties and is, therefore, beyond our control. Our VoIP service (and to a lesser extend our e-commerce services) requires our customers to have an operative broadband Internet connection and an electrical power supply, which are provided by the customer’s Internet service provider and electric utility company and not by us. The quality of some broadband Internet connections may be too poor for customers to use our services properly. In addition, if there is any interruption to a customer’s broadband Internet service or electrical power supply, that customer will be unable to make or receive calls, including emergency calls (our E-911 service), using our service. We outsource several of our network functions to third-party providers. If our third-party service providers fail to maintain these facilities properly, or fail to respond quickly to problems, our customers may experience service interruptions. The failure of any of these third party service providers to properly maintain services may be subject to factors including but not limited to the following: (i) cause a loss of customers, (ii) adversely affect our reputation, (iii) cause negative publicity, (iv) negatively impact our ability to acquire customers, (v) negatively impact our revenue and profitability, (vi) potential law suits for not reaching E-911 services, and (vii) potential law suits for loss of business and loss of reputation.

We rely on third parties to provide a portion of our customer service responses, initiate local number portability for our customers and provide aspects of our E-911 service.

We offer our telephony customers support 24 hours a day, seven days a week. We rely on third parties (sometimes outside of the U.S) to provide some services that respond to customer inquiries. These third-party providers generally represent us without identifying themselves as independent parties. The ability of third-party providers to provide these representatives may be disrupted due to issues outside our control.

We also maintain an agreement with an E-911 provider to assist us in routing emergency calls directly to an emergency service dispatcher at the PSAP in the area of the customer's registered location and terminating E-911 calls. We also contract with a provider for the national call center that operates 24 hours a day, seven days a week to receive certain emergency calls and with several companies that maintain PSAP databases for the purpose of deploying and operating E-911 services. The dispatcher will have automatic access to the customer's telephone number and registered location information. If a customer moves their Crexendo service to a new location, the customer's registered location information must be updated and verified by the customer. Until that takes place, the customer will have to verbally advise the emergency dispatcher of his or her actual location at the time of an emergency 9-1-1 call. This can lead to delays in the delivery of emergency services

Interruptions in service from these vendors could also cause failures in our customers' access to E-911 services and expose us to liability.

We also have agreements with companies that initiate our local number portability, which allow new customers to retain their existing telephone numbers when subscribing to our services. We will need to work with these companies to properly port numbers. The failure to port numbers may subject us to loss of customers or regulatory review.

If any of these third parties do not provide reliable, high-quality service, our reputation and our business will be harmed. In addition, industry consolidation among providers of services to us may impact our ability to obtain these services or increase our expense for these services.

Our dependence on outside contractors and third-party agents for fulfillment of certain items and critical manufacturing services could result in product or delivery delays and/or damage our customer relations.

We outsource the manufacturing of certain products we sell and products we provide. We submit purchase orders to agents or the companies that manufacture the products. We describe, among other things, the type and quantities of products or components to be supplied or manufactured and the delivery date and other terms applicable to the products or components. Our suppliers or manufacturers potentially may not accept any purchase order that we submit. Our reliance on outside parties involves a number of potential risks, including: (i) the absence of adequate capacity, (ii) the unavailability of, or interruptions in access to, production or manufacturing processes, (iii) reduced control over delivery schedules, (iv) errors in the product, and (v) claims of third party intellectual infringement or defective merchandise. If delays, problems or defects were to occur, it could adversely affect our business, cause claims for damages to be filed against us, and negatively impact our consolidated operations and cash flows.

Our success depends in part upon the capacity, reliability, and performance of our network infrastructure, including the capacity provided by our Internet bandwidth suppliers.

We depend on these companies to provide uninterrupted and error-free service. Some of these providers are also our competitors. We do not have control over these providers. We may be subject to interruptions or delays in network service. If we fail to maintain reliable bandwidth or performance that could significantly reduce customer demand for our services and damage our business.

Increased costs of third party suppliers may adversely affect our operating results.

Our contracts do not contain provisions allowing certain costs to be passed on to our customers. These include but are not limited to; power to our data center and capacity leased from our Internet bandwidth suppliers. We are not in control of costs for these services, or the reliability of these services. Failure of these providers could cause substantial harm to our costs and our ability to retain current customers and acquire new customers. A catastrophic failure of any of these systems could potentially subject us to liability.

Errors in our technology or technological issues outside our control could cause delays or interruptions to our customers.

Our services (including e-commerce and VoIP) may be disrupted by problems with our technology and systems such as malfunctions in our software or facilities. In addition there may be service interruptions for reasons outside our control. Our customers and potential customers subscribing to our services have experienced interruptions in the past and may experience interruptions in the future as a result of these types of problems. Interruptions could cause us to lose customers and offer customer credits, which could adversely affect our revenue and profitability. Network interruptions may also impair our ability to sign-up new customers. In addition since our systems and our customers' ability to use our services are Internet-dependent, our services may be subject to "hacker attacks" from the Internet, which could have a significant impact on our systems and services. Our customers' ability to use our services is dependent on third-party internet providers which may suffer service disruptions. If service interruptions adversely affect the perceived reliability of our service, we may have difficulty attracting and retaining customers and our growth may suffer.

Our operations could be hurt by a natural disaster, network security breach, or other catastrophic event.

We maintain a fully redundant network infrastructure in our data center in Tempe, Arizona. Currently, we do not have multiple site capacity if any catastrophic event occurs, although we expect to attain multiple site redundancy sometime in the future. This system does not guarantee continued reliability if a catastrophic event occurs. Despite implementation of network security measures, our servers may be vulnerable to computer viruses, break-ins, and similar disruptions from unauthorized tampering with our computer systems including, but not limited to, denial of service attacks. In addition, if there is a breach or alleged breach of security or privacy involving our services, or if any third party undertakes illegal or harmful actions using our communications or e-commerce services, our business and reputation could suffer substantial adverse publicity and impairment. We have experienced interruptions in service in the past. While we do not believe that we have lost customers as a consequence, the harm to our reputation is difficult to assess. We have taken and continue to take steps to improve our infrastructure to prevent service interruptions.

Failure in our data centers or services could lead to significant costs and disruptions.

All data centers, including ours, are subject to various points of failure. Problems with cooling equipment, generators, uninterruptible power supply, routers, switches, or other equipment, whether or not within our control, could result in service interruptions for our customers as well as equipment damage. Any failure or downtime could affect a significant percentage of our customers. The total destruction or severe impairment of our data center facilities could result in significant downtime of our services and the loss of customer data.

Internet security issues pose risks to the development of e-commerce and our business.

Security and privacy concerns may inhibit the growth of the Internet and other online services generally, especially as a means of conducting commercial transactions.

We could experience security breaches in the transmission and analysis of confidential and proprietary information of the consumer, the merchant, or both, as well as our own confidential and proprietary information.

Anyone able to circumvent security measures could misappropriate proprietary information or cause interruptions in our operations, as well as the operations of the merchant. We may be required to expend significant capital and other resources to protect against security breaches or to minimize problems caused by security breaches. To the extent that we experience breaches in the security of proprietary information which we store and transmit, our reputation could be damaged and we could be exposed to a risk of loss or litigation.

We depend on our senior management and other key personnel, and a loss of these individuals could adversely impact our ability to execute our business plan and grow our business.

We depend on the continued services of our key personnel, including our Officers and certain engineers. Each of these individuals have acquired specialized knowledge and skills with respect to our operations. The loss of one or more of these key personnel could negatively impact our performance. In addition, we expect to hire additional personnel as we continue to execute our strategic plan, particularly if we are successful in expanding our operations. Competition for the limited number of qualified personnel in our industry is intense. At times, we have experienced difficulties in hiring personnel with the necessary training or experience.

Evolving regulation of the Internet, including the use of e-mail as a marketing tool, may harm our business.
As e-commerce and VoIP continue to evolve, they are subject to increasing regulation by federal and state agencies. Areas subject to regulation include, but may not be limited to, the use of e-mail, user privacy, pricing, content, quality of products and services, taxation, advertising, intellectual property rights, and information security. In particular, our initial contact with some of our customers is through e-mail. The use of e-mail for this purpose has become the subject of a number of recently adopted and proposed laws and regulations. In addition, laws and regulations applying to the solicitation, collection, or processing of personal or consumer information could negatively affect our activities. The perception of security and privacy concerns, whether or not valid, may inhibit market acceptance of our products. In addition, legislative or regulatory requirements may heighten these concerns if businesses must notify website users that the data captured after visiting websites may be used by marketing entities to unilaterally direct product promotion and advertising to that user. Moreover, the applicability to the Internet of existing laws governing issues such as intellectual property ownership and infringement, copyright, trademark, trade secret, obscenity, and libel is uncertain and developing. Furthermore, any regulation imposing fees or assessing taxes for Internet use could result in a decline in the use of the Internet and the viability of e-commerce. Any new legislation or regulation, or the application or interpretation of existing laws or regulations, may decrease the growth in the use of the Internet, may impose additional burdens on e-commerce or may require us to alter how we conduct our business. This could decrease the demand for our products and services, increase our cost of doing business, increase the costs of products sold through the Internet, or otherwise have a negative effect on our business, results of operations, and financial position.

We depend upon our proprietary intellectual property rights, none of which can be completely safeguarded against infringement.

We rely upon copyright law, trade secret protection, and confidentiality or license agreements with our employees, customers, business partners, and others to protect our proprietary rights, but we cannot guarantee that the steps we have taken to protect our proprietary rights will be adequate. Although we have patents pending, we currently do not have any registered patents. Effective copyright, trademark, patent, and trade secret protections may not be able to be adequately protected in all Countries in which we operate source products or have an internet presence.

We may incur substantial expenses in defending against third-party patent and trademark infringement claims regardless of their merit.

From time to time, parties may assert patent infringement claims against us in the form of letters, lawsuits, and other forms of communication. Third parties may also assert claims against us alleging infringement of copyrights, trademark rights, trade secret rights or other proprietary rights or alleging unfair competition. If there is a determination that we have infringed third-party proprietary rights, we could incur substantial monetary liability and be prevented from using the rights in the future.

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Some provisions of our certificate of incorporation and bylaws may deter takeover attempts that may limit the opportunity of our stockholders to sell their shares at a favorable price.

Some of the provisions of our certificate of incorporation and bylaws could make it more difficult for a third party to acquire us, even if doing so might be beneficial to our stockholders by providing them with the opportunity to sell their shares at a premium to the then market price. Our bylaws contain provisions regulating the introduction of business at annual stockholders' meetings by anyone other than the board of directors. These provisions may have the effect of making it more difficult, delaying, discouraging, preventing or rendering more costly an acquisition or a change in control of our Company.

In addition, our corporate charter provides for a staggered board of directors divided into two classes. Provided that we have at least four directors, it will take at least two annual meetings to effectuate a change in control of the board of directors because a majority of the directors cannot be elected at a single meeting. This extends the time required to effect a change in control of the board of directors and may discourage hostile takeover bids. We currently have five directors.

Further, our certificate of incorporation authorizes the board of directors to issue up to 5,000,000 shares of preferred stock, which may be issued in one or more series, the terms of which may be determined at the time of issuance by the board of directors without further action by stockholders. Such terms may include voting rights, including the right to vote as a series on particular matters, preferences as to dividends and liquidation, conversion and redemption rights and sinking fund provisions. No shares of preferred stock are currently outstanding and we have no present plans for the issuance of any preferred stock. However, the issuance of any preferred stock could materially adversely affect the rights of holders of our common stock, and therefore could reduce its value. In addition, specific rights granted to future holders of preferred stock could be used to restrict our ability to merge with, or sell assets to, a third party. The ability of the board of directors to issue preferred stock could make it more difficult, delay, discourage, prevent, or make it more costly to effect a change in control, thereby preserving the current stockholders' control.

Our publicly filed SEC reports are reviewed by the SEC from time to time and any significant changes required as a result of any such review may result in material liability to us and have a material adverse impact on the trading price of our common stock.

The reports of publicly-traded companies are subject to review by the SEC from time to time for the purpose of assisting companies in complying with applicable disclosure requirements and to enhance the overall effectiveness of companies' public filings. Comprehensive reviews by the SEC of such reports are now required at least every three years under the Sarbanes-Oxley Act of 2002. SEC reviews often occur at the time companies file registration statements, but reviews may be initiated at any time by the SEC. While we believe that our previously filed SEC reports comply, and we intend that all future reports will comply, in all material respects with the published rules and regulations of the SEC, we could be required to modify or reformulate information contained in prior filings as a result of an SEC review. Any modification or reformulation of information contained in such reports could be significant and result in a material liability to us and have a material adverse impact on the trading price of our common stock.

Examinations by relevant tax authorities may result in material changes in related tax reserves for tax positions taken in previously filed tax returns or may impact the valuation of certain deferred income tax assets, such as net operating loss carry-forwards.

Based on the outcome of examinations by relevant tax authorities, or as a result of the expiration of statutes of limitations for specific jurisdictions, it is reasonably possible that the related tax reserves for tax positions taken regarding previously filed tax returns will materially change from those recorded in our financial statements. In addition, the outcome of examinations may impact the valuation of certain deferred income tax assets (such as net operating loss carry-forwards) in future periods. It is not possible to estimate the impact of the amount of such changes, if any, to previously recorded uncertain tax positions.

We may undertake acquisitions, mergers or change to our capital structure to expand our business, which may pose risks to our business and dilute the ownership of our existing stockholders.

As part of a potential growth strategy we may attempt to acquire or merge with certain businesses. Whether we realize benefits from any such transactions will depend in part upon the integration of the acquired businesses, the performance of the acquired products, services and capacities of the technologies acquired, as well as the personnel hired in connection therewith. Accordingly, our results of operations could be adversely affected from transaction-related charges, amortization of intangible assets, and charges for impairment of long-term assets. While we believe that we have established appropriate and adequate procedures and processes to mitigate these risks, there can be no assurance that any potential transaction will be successful.

In addition, the financing of any acquisition may require us to raise additional funds through public or private sources. Additional funds may not be available on terms that are favorable to us and, in the case of equity financings, may result in dilution to our stockholders. Future acquisitions by us could also result in large and immediate write-offs or assumptions of debt and contingent liabilities, any of which may have a material adverse effect on our consolidated financial position, results of operations, and cash flows.

We collect personal and credit card information from our customers and employees could misuse this information.

We maintain credit card and other personal information in our systems. Due to the sensitive nature of retaining such information we have implemented policies and procedures to preserve and protect our data and our customers’ data against loss, misuse, corruption, misappropriation caused by systems failures, unauthorized access, or misuse. Notwithstanding these policies, we could be subject to liability claims by individuals and customers whose data resides in our databases for the misuse of that information.

ITEM 2. PROPERTIES

Our corporate offices consist of approximately 22,000 square feet of office space in Tempe, Arizona owned by our owner and CEO and approximately 1,300 square feet of office space in Reno, NV which is leased from unaffiliated third parties. Our corporate office is located at 1615 South 52nd Street, Tempe, Arizona 85281. During the year ended December 31, 2012, we recorded a $1,393,042 impairment charge related to the abandonment of office space under an operating lease in Orem, UT (See Note 6). We maintain tenant fire and casualty insurance on our assets located in these buildings in an amount that we deem adequate.

ITEM 3. LEGAL PROCEEDINGS

From time to time we receive inquiries from federal, state, city and local government officials in the various jurisdictions in which we operate. These inquiries and investigations generally concern compliance with various city, county, state, and/or federal regulations involving sales, representations made, customer service, refund policies, and marketing practices. We respond to these inquiries and have generally been successful in addressing the concerns of these persons and entities, without a formal complaint or charge being made, although there is often no formal closing of the inquiry or investigation. There can be no assurance that the ultimate resolution of these or other inquiries and investigations will not have a material adverse effect on our business or operations, or that a formal complaint will not be initiated. We also receive complaints and inquiries in the ordinary course of our business from both customers and governmental and non-governmental bodies on behalf of customers, and in some cases these customer complaints have risen to the level of litigation. There can be no assurance that the ultimate resolution of these matters will not have a material adverse effect on our business or results of operations.

On November 4, 2013, the Company received a motion for leave to file an amended complaint and a request for scheduling conference (including a request for extending discovery) in the case entitled INFORMATION TECHNOLOGY CUSTOMER CARE, INC., Plaintiff v STORESONLINE, INC., Defendant; filed in IN THE FOURTH DISTRICT COURT, UTAH COUNTY, and STATE OF UTAH Case No. 090401169. In the original Complaint, Plaintiff ITCCI claimed that StoresOnline breached a contract with ITCCI by improperly moving its Philippine support to a new support center. ITCCI also alleged an action for tortious interference claiming that StoresOnline caused former employees of ITCCI to leave to work for that support center. There was also a claim for “civil conspiracy”. The original Complaint sought actual and punitive damages.

The parties had completed discovery and filed various motions, including a motion for Summary Judgment by StoresOnline. The Company believes there was no evidence to support any of the claims raised by the Plaintiff, and that there was no contractual obligation which would have prohibited a change of support centers.

The Plaintiff has filed motions to substitute new counsel, amend its Complaint and re-open discovery. The allegations included in the proposed Amended Complaint are that former officers and executives of StoresOnline acted fraudulently and secretly to improperly move support centers. The Company strongly disputes the allegations against it under both the original Complaint and the proposed Amended Complaint. Moreover, even if any of the allegations regarding former employees in the proposed Amended Complaint were true, the Company believes that it would have no liability for those alleged actions.

On February 8, 2013 the Company received a summons entitled TCU - Canyon Park, a Utah Limited Company, Plaintiff (TCU) v Crexendo, Inc. a Delaware Corporation F/K/A iMergent, Inc., Defendant. The Suit was filed in the Fourth Judicial District Court of Utah County, Provo Department. The Suit seeks unspecified damages against the company for vacating a lease premises. The suit claims that the Company owes basic monthly rent of $112,454 from November 2012 through October 2013 together with other charges (including C.A.M., late fees, property damages, and interest and attorney fees). The Plaintiff alleges that the Company "quit" the premises in November 2012 and the lease terminates in October 2013.

The Company vacated the premises in November 2012, and alleges it did so due to violations of TCU. The Company had notified TCU that the premises were not habitable and that TCU had violated the Companies rights regarding possession and was therefore vacating the premises.

On March 29, 2013 the Company and TCU resolved all outstanding issues and the case was dismissed with prejudice.

We are also subject to various claims and legal proceedings covering matters that arise in the ordinary course of business. We believe that the resolution of these other cases will not have a material adverse effect on our business, financial position, or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES

The disclosure required by this item is not applicable

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

MARKET INFORMATION

Our common stock began trading on the NYSE - MKT on August 16, 2004 under the symbol "IIG." The following table sets forth the range of high and low sales prices as reported on the NYSE – MKT for the periods indicated. In May 2011, our stockholders approved an amendment to our Certificate of Incorporation to change our name from "iMergent, Inc." to "Crexendo, Inc." The name change was effective May 18, 2011. Our ticker symbol "IIG" on the New York Stock Exchange wasd>

572,250

58,871

(7)

1,474,480

Michael Vesey (3) (9)

2017

175,000

(8)

302,500

51,330

12,178

(7)

541,008

Vice President and Chief

Financial Officer

2016

43,750

12,500

56,250

William Botti (4)

2017

225,000

139,740

17,118

(7)

381,858

Executive Vice President of Sales

2016

225,000

215,378

183,086

15,037

(7)

638,501

2015

225,000

203,832

169,175

11,220

(7)

609,227

Vito Legrottaglie (5) (9)	
	2017
	200,000
	124,500
	102,660
	15,232
(7)	
	442,392
Vice President Chief	

2016

200,000

20,917

104,481

119,083

15,174

(7)

459,655

Information Officer

2015

200,000

101,916

107,675

15,755

(7)

425,346

Brian Gilbertson (6) (9)

2017

175,000

132,800

139,983

4,296

(7)

452,079

Vice President and General Manager Lifeboat

2016

175,000

225,225

115,000

(7)

515,225

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(1) The amount included in Stock Awards is the aggregate grant date fair value computed in accordance with FASB ASC Topic 718 (formerly FAS 123R). See Note 6, Stockholder s Equity and Stock Based Compensation in the Company s consolidated financial statements set forth in our Annual Report on Form 10-K for the assumptions made in determining stock award values.

(2) Mr. Nynens also serves as the Chairman of the Board of Directors but does not receive any compensation for his service in this capacity.

(3) Mr. Vesey was appointed Vice President and Chief Financial Officer in October 2016. Compensation presented for 2016 represents the period from appointment to December 31, 2016.

(4) Mr. Botti was appointed Executive Vice President of Sales on April 21, 2014 and served in such capacity until his retirement on December 31, 2017.

(5) Mr. Legrottaglie was appointed Vice President and Chief Information Officer in February 2015 after having served as Vice President of Operations and Information Systems since April 2007.

(6) Mr. Gilbertson was appointed Vice President and General Manager of Lifeboat in May 2016 after having served as Vice President of Business Development since May 2015.

(7) A detailed description of the items disclosed as All-Other Compensation is set forth in the table below.

(8) 2016 includes a periodic grant of 100,000 shares of Restricted Stock to Mr. Nynens which vests over twenty quarters. 2017 includes an initial employment grant of 10,000 shares of Restricted Stock to Mr. Vesey which vests over sixteen quarters.

(9) In February 2018, the Compensation Committee approved annual salary increases of $50,000 to Mr. Nynens and Mr. Vesey, and $25,000 to Mr. Legrottaglie and Mr. Gilbertson, effective January 1, 2018.

All Other Compensation

Name		401(k) Matching Contributions ($)	Dividend Equivalents On Unvested Restricted Stock ($)	Personal Use of Company Car ($)	Supplemental Life Insurance Premiums ($)	Total ($)
Simon Nynens	2017	8,813	83,637	4,201	4,310	100,961
	2016	9,000	93,687	4,534	4,310	111,531
	2015	9,000	39,610	5,951	4,310	58,871
Michael Vesey	2017	6,228	5,950			12,178
	2016					
William Botti	2017		17,118			17,118
	2016		15,037			15,037
	2015		11,220			11,220
Vito Legrottaglie	2017	7,727	7,505			15,232
	2016	7,724	7,450			15,174
	2015	9,125	6,630			15,755
Brian Gilbertson	2017		4,296			4,296
	2016					

GRANT OF PLAN-BASED AWARDS

The following table shows information regarding awards granted to each of our Named Executive Officers under our Executive Plan and 2012 Plan during 2017.

		Estimated future payouts under non-equity incentive plan awards (1)			Estimated future payouts under equity incentive plan awards (2)			All other Stock Awards Number: of Shares	Grant Date Fair Value of Stock Awards (3)
		Threshold	Target	Maximum	Threshold	Target	Maximum		
Name	Grant Date	($)	($)	($)	(#)	(#)	(#)	(#)	($)
Simon Nynens	2/1/2017	234,000	803,000	950,000	26,274	31,057	32,000		473,100
Michael Vesey	2/1/2017	19,500	74,650	100,000	6,710	7,931	8,000		124,500
	2/7/2017							10,000	178,000
William Botti	2/1/2017	39,000	277,500	400,000					
Vito Legrottaglie	2/1/2017	32,000	154,500	200,000	6,710	7,931	8,000		124,500
Brian Gilbertson	2/1/2017	32,500	155,000	330,000	6,710	7,994	8,000		132,800

(1) These amounts represent target threshold, target and maximum awards established under our Executive Plan. The actual amount of each award authorized for payment by our Compensation Committee in February 2018 is included in the 2017 Summary Compensation Table above under the heading Non-Equity Incentive Compensation.

(2) These amounts represent threshold, target and maximum awards of Restricted Stock awards granted under our Executive Plan. The actual grant date fair value computed in accordance with FASB ASC Topic 718 of each award authorized for issuance by our Compensation Committee in February 2017 is included in the Summary Compensation Table above under the heading Stock Awards. Fair value of performance-based Restricted Stock Awards is calculated using the closing stock price on the date of the grant, based on the probable outcome of the performance conditions.

(3) These amounts represent the actual amount of each award of Restricted Stock authorized for issuance by our Compensation Committee in February 2018 and included in the 2017 Summary Compensation Table above under the heading Stock Awards .

Options Exercised and Stock Vested in 2017

The table below shows the number of shares of Common Stock acquired during 2017 upon the exercise of options and vesting of Restricted Stock.

	Option Awards		Stock Awards	
Name	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise ($)	Number of Shares Acquired On Vesting (#)	Value Realized On Vesting ($)
Simon Nynens			43,100	738,088
Michael Vesey			2,000	34,250
William Botti			9,790	167,658
Vito Legrottaglie			5,652	98,073
Brian Gilbertson			2,884	49,397

Outstanding Equity Awards

The following table shows the number of shares of Common Stock covered by exercisable and unexercisable options and unvested Restricted Stock held by the Company s Named Executive Officers on December 31, 2017.

Outstanding Equity Awards at December 31, 2017

	Option Awards				Stock Awards	
Name	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price ($)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#) (1)	Market Value of Shares or Units of Stock That Have Not Vested ($) (2)
Simon Nynens					105,700	1,765,190
Michael Vesey					8,000	133,600
William Botti					2,446	40,848
Vito Legrottaglie					9,120	152,304
Brian Gilbertson					8,616	143,887

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(1) In February 2017, Messrs. Nynens, Botti, Legrottaglie, and Gilbertson were awarded 30,000, 11,750, 5,700, and 7,500 shares of Restricted Stock, respectively, based on achieving operating income goals under the 2016 bonus plan. The Restricted Stock vests over 16 equal quarterly installments. In February 2017, Mr. Vesey was awarded an initial employment grant of 10,000 shares of Restricted Stock, and the Restricted Stock vests over 20 equal quarterly installments. In February 2016, Messrs. Nynens, Botti and Legrottaglie were awarded 30,400, 11,400 and 5,700 shares of Restricted Stock, respectively, based on achieving operating income goals under the 2015 bonus plan. The Restricted Stock vests over 16 equal quarterly installments. In February 2016, Messrs. Nynens and

Gilbertson were awarded 100,000 and 5,000 shares of Restricted Stock, respectively, and the Restricted Stock vests over 20 equal quarterly installments. Mr. Nynens grant of 100,000 shares of Restricted Stock was a retention award, the last such award was made to Mr. Nynens in January 2006 and vested over 10 years. In February 2015, Messrs. Nynens and Legrottaglie were awarded 32,000 and 8,000 shares of Restricted Stock, respectively. The Restricted Stock vests over 16 equal quarterly installments. In 2014, Mr. Botti was awarded 20,000 shares of Restricted Stock under the terms of his employment agreement. The Restricted Stock vests over 20 equal quarterly installments.

(2) The market value is based on the closing stock price of the Company s Common Stock of $16.70 on December 29, 2017, the last trading day of 2017.

Employment and Severance Agreements

Each of the Named Executive Officers has entered into an agreement that includes a covenant not-to-compete and a confidentiality provision. The covenant not-to-compete prohibits the executive from engaging in a competing business for a period of one year after termination. Such covenant also prohibits the executive from directly or indirectly soliciting the Company s customers or employees.

On January 9, 2006, the Company appointed Simon Nynens to be its President and Chief Executive Officer and entered into a related employment agreement with Mr. Nynens, dated as of January 12, 2006. The agreement provides for an initial base salary of $250,000, subject to increase at the discretion of the Compensation Committee, and a bonus, pursuant to a bonus plan adopted by the Board of Directors. Additionally, after approval of the 2006 Plan (defined above), Mr. Nynens was awarded 200,000 shares of Restricted Stock in connection with his appointment, which shares vest in 40 equal quarterly installments.

In the event that Mr. Nynens employment is terminated without cause or by the rendering of a non-renewal notification, he is entitled to receive severance payments equal to twelve months cash compensation, immediate vesting of all outstanding equity awards, and to purchase the car used by him at the buy-out price of any lease or fair market value, as applicable. Additionally, in the event that a change of control of the Company occurs (as described below under Potential Payments Upon Termination or Change of Control), Mr. Nynens outstanding equity awards become immediately vested and he is entitled to receive a lump-sum payment equal to 2.9 times his then annual salary and actual incentive bonus earned in the year prior to such change in control.

On January 6, 2003, the Company entered into a severance agreement with Mr. Legrottaglie, Vice President of Chief Information Officer, under which Mr. Legrottaglie is entitled to severance payments for six months at the then applicable annual base salary if the Company terminates his employment for any reason other than for cause.

In October 2016, the Company entered into a severance agreement with Mr. Vesey, Vice President and Chief Financial Officer, under which Mr. Vesey is entitled to severance payments for six months at the then applicable annual base salary if the Company terminates his employment for any reason other than for cause. Additionally, in the event that a change of control of the Company occurs (as described below), the Chief Financial Officer s outstanding equity awards become immediately vested and he is entitled to receive a lump-sum payment equal to 1.0 times his then current annual salary and actual incentive bonus earned in the year prior to such change in control.

The payments triggered by such terminations pursuant to Mr. Nynens, Mr. Vesey, and Mr. Legrottaglie s respective employment agreements, as well as those triggered by a change of control under the employment agreements of all Named Executive Officers, are illustrated in tabular format under Potential Payments Upon Termination or Change of Control below.

Potential Payments Upon Termination or Change in Control

The Company has entered into certain agreements and maintains certain plans that require the Company to provide compensation to the Named Executive Officers in the event of a termination of employment or a change in control of the Company. The amount of compensation to each Named Executive Officer in each situation is listed in the tables below. The amounts shown assume that such termination or change of control was effective on December 31, 2017 and that the Company s stock was $16.70 per share, which was the closing price of the shares on

December 29, 2017 (the last trading day of 2017).

The following table illustrates the payments that would be due to the Named Executive Officers in the event of a change of control of the Company. For purposes hereof, a change of control shall be deemed to have occurred in the event of any of the following: (i) any person or entity makes a tender or exchange offer for shares of the Common Stock pursuant to which such person or entity acquires a majority of the issued and outstanding shares of the Common Stock, (ii) the Company merges or consolidates with or into another corporation or corporations, unless immediately after such merger or consolidation those persons and entities who immediately prior to such transaction were stockholders of the Company are entitled to vote in the election of directors, or otherwise have the right to elect, a majority of the directors of the surviving corporation, (iii) the Company sells, transfers or otherwise disposes of all or substantially all of its assets, other than to a direct or indirect subsidiary, or (iv) any person or entity acquires a majority of the Company s issued and outstanding voting securities and shall be entitled to vote in the election of directors or otherwise have the right to elect, a majority of the directors of the Company.

Name	Lump Sum Payment Based on Salary ($)	Lump Sum Payment Based on Bonus ($)	Accelerated Vesting on Restricted Stock ($)	Total ($)
Simon Nynens	870,000	1,162,867	1,765,190	3,798,058
Michael Vesey	175,000	51,330	133,600	359,930
William Botti			40,848	40,848
Vito Legrottaglie			152,304	152,304
Brian Gilbertson			143,837	143,837

The following table illustrates the payments that would be due the Named Executive Officers in the event they are terminated without cause, and with respect to Mr. Nynens, also upon receipt of non-renewal notification. For purposes hereof, cause is defined as (A) the commission by the executive of a felony or an offense involving moral turpitude, the executive s engaging in theft, embezzlement, fraud, obtaining funds or property under false pretenses, or similar acts of misconduct with respect to the property of the Company or its employees, stockholders, affiliates, customers, licensees, licensors or suppliers, (B) the repeated failure by the executive to perform his duties under his employment agreement or comply with reasonable policies or directives of the Board of Directors, or (C) the material breach of the employment agreement or the conditions of employment.

Name	Payment Based On Salary ($)	Bonus($)	Accelerated Vesting on Restricted Stock ($)	Accelerated Vesting on Stock Options ($)	Total ($)
Simon Nynens	300,000		1,765,199		2,065,199
Michael Vesey	87,500				87,500
William Botti					
Vito Legrottaglie	100,000				100,000
Brian Gilbertson					

The severance payments disclosed above are to be made to Mr. Nynens in twelve consecutive equal monthly installments and to Messrs. Vesey, and Legrottaglie in one lump-sum payment.

Pay Ratio

Recent SEC rules require us to disclose the ratio of the annual total compensation of our Chief Executive Officer to the median of the annual total compensation of our other employees. In determining the median annual total compensation of our other employees, we prepared a list of all employees as of December 31, 2017. Consistent with applicable rules, we used reasonable estimates both in the methodology used to identify the median employee and in calculating the annual total compensation of employees other than the Chief Executive Officer. We determined our median employee based on the taxable wages of each of our employees (excluding the Chief Executive Officer). We annualized the taxable wages of employees who joined the Company during 2017.

The annual total compensation of our median employee (other than the Chief Executive Officer) for 2017 was $51,119. As disclosed in the Summary Compensation Table appearing on page 18, our Chief Executive Officer s annual total compensation for 2017 was $1,275,050. Based on the foregoing, our estimate of the ratio of the annual total compensation of our Chief Executive Officer to the median of the annual total compensation of all other employees was approximately 25 to 1. Given the different methodologies that various public companies will use to determine an estimate of their pay ratio, the estimated ratio reported above should not be used as a basis for comparison between companies.

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PROPOSAL 2

ADVISORY VOTE TO APPROVE OUR EXECUTIVE COMPENSATION

General

The Dodd-Frank Wall Street Reform and Consumer Protection Act requires us to obtain an advisory vote (non-binding) from our stockholders on our executive compensation as disclosed in this proxy statement, which is often referred to as a say on pay proposal, at least once every three years.

As described in the Compensation Discussion and Analysis section of this proxy statement, our executive compensation programs and policies play an important role in achieving our objective of sustainable long-term growth in stockholder value. As a guiding principle, our executive compensation programs and policies are designed to motivate, retain and reward our executives for superior short- and long-term performance for the Company and its stockholders.

We are asking that our stockholders indicate their support of our executive compensation as described in this proxy statement. While this advisory vote on executive compensation is non-binding, our Board and the Compensation Committee will review the outcome of this vote and take the vote into consideration when reviewing our compensation policies and procedures. This is not intended to address specific items of compensation, but rather the overall compensation of our Named Executive Officers and our executive compensation policies and procedures as described in this proxy statement. Stockholders who want to communicate with our Board of Directors should refer to Communications with the Board of Directors in this proxy statement for additional information.

At the Annual Meeting we will ask our stockholders to approve the following resolution:

RESOLVED, that the Company s stockholders approve, on an advisory basis, the compensation of the Named Executive Officers, as described in the Company s proxy statement for the 2018 Annual Meeting of Stockholders pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including the Compensation Discussion and Analysis, the 2017 Summary Compensation Table and the other compensation related tables and disclosure.

THE BOARD OF DIRECTORS RECOMMENDS THAT STOCKHOLDERS VOTE FOR THE APPROVAL OF THE COMPANY S EXECUTIVE COMPENSATION AS DESCRIBED IN THIS PROXY STATEMENT.

PROPOSAL 3

VOTE TO APPROVE AN AMENDMENT TO OUR 2012 STOCK-BASED COMPENSATION PLAN TO AUTHORIZE AN INCREASE IN NUMBER OF SHARES AVAILABLE FOR AWARDS THEREUNDER

Background

Our 2012 Plan allows us to grant equity awards to our employees, officers and directors. We believe that our continued success depends on attracting and retaining the highest caliber employees. The ability to grant equity awards pursuant to our 2012 Plan is a crucial tool that the Company can use when recruiting new personnel and incentivizing and retaining our current personnel.

Our executive compensation programs and policies play an important role in achieving our objective of sustainable long-term growth in stockholder value. As a guiding principle, our executive compensation programs and policies are designed to motivate, retain and reward our executives for superior short- and long-term performance for the Company and its stockholders.

Summary of the Proposal

We are asking our stockholders to approve an amendment to our 2012 Plan to increase the number of shares of Common Stock authorized thereunder, from 600,000 to 1,000,000, and to increase the number of shares available for new grants thereunder to our employees, officers and directors, from 185,346 to 585,346.

At the Annual Meeting we will ask our stockholders to approve the following resolution:

RESOLVED, that the Company s stockholders approve an amendment to our 2012 Stock-Based Compensation Plan to an increase in the number of shares of Common Stock authorized for grant thereunder from 600,000 to 1,000,000.

The Importance of Proposed Increases

The Board believes that in it is the best interests of the Company and its stockholders to have the continued ability to grant equity awards to current and potential employees, officers and directors. Equity awards allow the company to attract and maintain talented personnel. The inability to attract and maintain talented personnel could hinder the Company s ability to operate its business and achieve sustainable long-term growth in stockholder value. An inability to offer equity awards also means the Company would have to consider offering its personnel additional cash-based awards.

Share Information

As of April 6, 2018, the 2012 Plan had 199,209 shares subject to vesting under outstanding Restricted Stock awards and 185,346 shares available for future issuance, of which approximately 75,000 to 169,000 shares are issuable based on the outcome of certain performance conditions contained in 2018 incentive stock grants, and other new hire grants.

THE BOARD OF DIRECTORS RECOMMENDS THAT STOCKHOLDERS VOTE FOR THE APPROVAL OF THE AMENDMENT TO OUR 2012 PLAN TO INCREASE THE NUMBER OF SHARES AVAILABLE TO BE GRANTED UNDER OUR 2012 PLAN.

PROPOSAL 4

RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Our independent registered public accounting firm during the year ended December 31, 2017 was EisnerAmper LLP. EisnerAmper LLP and its predecessor, Amper, Politziner & Mattia, LLC, have audited our financial statements since 2002. The Audit Committee has appointed EisnerAmper LLP to serve as the Company s independent registered public accounting firm for 2018. While we are not required to have the stockholders ratify the selection of EisnerAmper LLP as our independent auditors, we are doing so because we believe it is a matter of good corporate practice. If the stockholders do not ratify the selection, the Audit Committee will reconsider whether or not to retain EisnerAmper LLP; however, the Audit Committee will not be under any obligation to adhere to the stockholders vote on this proposal, and in its full discretion may choose to maintain EisnerAmper LLP as the Company s independent registered public accounting firm. Even if the selection is ratified, the Audit Committee, in its discretion, may change the appointment at any time during the year if it determines that such a change would be in the best interests of the Company and its stockholders.

One or more representatives of EisnerAmper LLP are expected to be present at the meeting. They will have the opportunity to make a statement and will be available to respond to appropriate questions.

Fees and Independence

Audit Fees, Audit-Related Fees and Tax Fees

The following table sets forth the fees billed by our independent registered public accountants for each of our last two fiscal years for the categories of services indicated.

Category		**2017**		**2016**
Audit Fees - (1)	$	210,000	$	176,000
Tax Fees - (2)	$		$	22,000
Audit-Related Fees (3)	$	23,000	$	27,000

(1) Consists of fees billed for the audit of our annual financial statements, review of interim financial statements included in our Quarterly Reports on Form 10-Q and services that are normally provided by the auditors in connection with statutory and regulatory filings, including registration statements and consents.

(2) Consists of services for tax compliance and tax advice.

(3) Consist of services not directly related to the audit of the Company s financial statements which includes audits of benefit plans.

The Audit Committee has determined that the provision of services by EisnerAmper LLP described in the preceding paragraphs is compatible with maintaining EisnerAmper LLP independence. All permissible audit and non-audit services provided by EisnerAmper LLP in 2016 and 2017 were pre-approved by the Audit Committee on a case-by-case basis.

THE BOARD RECOMMENDS THAT YOU VOTE FOR THE RATIFICATION OF EISNERAMPER LLP AS THE COMPANY S INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM FOR 2018.

GENERAL

The Company does not know of any matters other than those stated in this proxy statement which are to be presented for action at the Meeting. If any other matters should properly come before the Meeting, proxies will be voted on these other matters in accordance with the judgment of the persons voting the proxies. Discretionary authority to vote on such matters is conferred by such proxies upon the persons designated therein as proxy appointees. The Company will bear the cost of preparing, printing, assembling and mailing all proxy material which may be sent to stockholders in connection with this solicitation. Arrangements will also be made with brokerage houses, other custodians, nominees and fiduciaries, to forward soliciting material to the beneficial owners of the Company s Common Stock held by such persons. The Company will reimburse such persons for reasonable out-of-pocket expenses incurred by them. In addition to the solicitation of proxies by use of the mails, officers and regular employees of the Company may solicit proxies without additional compensation, by telephone, telecopy or telegraph. The Company does not expect to pay its officers or employees any compensation for the solicitation of proxies.

TRANSACTIONS WITH RELATED PERSONS

The Company has adopted a written policy whereby all transactions between the Company and each related person (as defined in Item 404 of Regulation S-K) or in which any related person had or will have a direct or indirect material interest must be on terms no less favorable to the Company than could be obtained from unrelated third parties and require pre-approval by a majority of the disinterested members of the Company s Board of Directors. There have been no such transactions since January 1, 2006.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

F. Duffield Meyercord, Mike Faith, Steve DeWindt and Diana Kurty served as members of the Compensation Committee during the last completed fiscal year. None of Messrs. Meyercord, Faith, or DeWindt or Ms. Kurty (i) was, during the last completed fiscal year, an officer or employee of the Company or any of its subsidiaries, (ii) was formerly an officer of the Company or any of its subsidiaries, or (iii) had any relationship requiring disclosure by the Company under any paragraph of Item 404 of Regulation S-K. Furthermore, no executive officer and no member of the Committee had a relationship that requires disclosure under Item 407(e)(4)(iii) of Regulation S-K.

COMPENSATION COMMITTEE REPORT

The Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis set forth above with management. Based on the review and discussion, the Compensation Committee has recommended to the full Board of Directors that the Compensation Discussion and Analysis be included in this proxy statement for filing with the SEC.

<u>The Committee</u>

Mike Faith, Chairman

Steve DeWindt

Diana Kurty

Jeffrey R. Geygan

REPORT OF THE AUDIT COMMITTEE

In the course of fulfilling its responsibilities during fiscal year 2017, the Audit Committee of our Board of Directors has:

- reviewed and discussed with management our audited financial statements for the year ended December 31, 2017;

- discussed with representatives of EisnerAmper LLP (the Independent Registered Public Accounting Firm) the matters required to be discussed by Statement on Auditing Standards No. 61, Communication with Audit Committees, as amended, as adopted by the Public Company Accounting Oversight Board in Rule 3200T;

- received the written disclosures and the letter from the Independent Registered Public Accounting Firm required by Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees, as amended;

- discussed with the Independent Registered Public Accounting Firm its independence from the Company and management; and

- considered whether the provision by the Independent Registered Public Accounting Firm of non-audit services is compatible with maintaining the Independent Registered Public Accounting Firm s independence.

Based on the foregoing, the Audit Committee recommended to the Board of Directors that the audited financial statements referred to above be included in the Company s Annual Report on Form 10-K for the year ended December 31, 2017 for filing with the SEC.

Respectfully submitted,
Diana Kurty, Chair
Mike Faith
Steve DeWindt
Jeffrey R. Geygan

Householding

Beneficial owners of Common Stock who share a single address may receive only one copy of the Notice or the proxy materials, as the case may be, unless their broker, bank or nominee has received contrary instructions from any beneficial owner at that address. This practice, known as householding, is designed to reduce printing and mailing costs. If any beneficial shareowner(s) at such an address wish to discontinue householding and receive a separate copy of the Notice or the proxy materials, as the case may be, or if they currently receive multiple copies at the same address and wish to receive only a single copy in the future, they may contact Broadridge, either by calling (800) 579-1639, or by writing to Broadridge, Household Department, 51 Mercedes Way, Edgewater, New York, 11717.

STOCKHOLDER PROPOSALS FOR INCLUSION IN THE COMPANY S 2019 ANNUAL MEETING PROXY STATEMENT AND PROXY CARD

Any stockholder proposal to be considered by us for inclusion in the Company s 2019 proxy statement and form of proxy card for next year s Annual Meeting of Stockholders, expected to be held in June 2019, must be received by the Company s Corporate Secretary at the Company s principal executive offices located at 4 Industrial Way West, 3rd Floor, Eatontown, NJ 07724, no later than December 21, 2018 (120 days prior to the first anniversary of the date of this proxy statement): provided that, if the Company provides less than 60 days notice or prior public disclosure of the date of the 2018 Annual Meeting of Stockholder, to be timely, any such stockholder proposal must be received no later than the close of business on the tenth day following the day on which such notice or prior disclosure was made, whichever first occurs. The SEC rules set forth standards as to what stockholder proposals are required to be included in a proxy statement.

OTHER STOCKHOLDER PROPOSALS FOR PRESENTATION AT THE COMPANY S 2019 ANNUAL MEETING

For any proposal that is not submitted for inclusion in next year s proxy statement by the deadline identified above, SEC rules permit management to vote proxies in its discretion if the Company: (a) receives notice of the proposal more than 45 days prior to the anniversary of the mailing date of this proxy statement and the Company advises stockholders in next year s proxy statement about the nature of the matter and how management intends to vote on such matter, (subject to the right of the proposing stockholder to deliver a proxy statement and proxy of its own in compliance with the terms of Rule 14a-4(c)(2) under the Exchange Act), or (b) does not receive notice of the proposal at least 45 days prior to the anniversary of the mailing date of this proxy statement. Notices of intention to present proposals at the 2019 annual meeting should be addressed to the Company s Corporate Secretary at the Company s principal executive offices located at 4 Industrial Way West, 3rd Floor, Eatontown, NJ 07724.

By Order of the Board of Directors,

Simon F. Nynens, Chairman
April 20, 2018

PROXY CARD

WAYSIDE TECHNOLOGY GROUP, INC.

4 Industrial Way West, 3rd Floor

Eatontown, New Jersey 07724

THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS

The undersigned hereby appoints SIMON F. NYNENS and KEVIN T. SCULL with the power to appoint their substitutes, and hereby authorizes them to represent and to vote on behalf of the undersigned all the shares of common stock, par value $.01 per share (the Common Stock), of Wayside Technology Group, Inc., that the undersigned would be entitled to vote if personally present at the Annual Meeting of Stockholders to be held at the Company s headquarters, 4 Industrial Way West, 3rd Floor, Eatontown, New Jersey 07724, on June 6, 2018 at 10:00 AM local time or any adjournment or adjournments thereof, hereby revoking all proxies heretofore given with respect to such shares, upon the following proposals more fully described in the notice of and proxy statement for the Meeting (receipt whereof is hereby acknowledged, and with discretionary authority with respect to such other matters as may properly come before such meeting or any adjournment or adjournments thereof).

1. ELECTION OF DIRECTORS

o **FOR** all nominees listed below

o **WITHHOLD AUTHORITY** to vote for nominees listed below (except as marked to the contrary below)

NOMINEES: SIMON F. NYNENS, MIKE FAITH, STEVE DEWINDT, DIANA KURTY, AND JEFFREY GEYGAN

(INSTRUCTION: To withhold authority to vote for any one or more nominees, write the name(s) of such nominee(s) name in the space provided below)

Vote on Proposals	**For**	**Against**	**Abstain**
2. Advisory vote to approve the compensation of the Company s Named Executive Officers	o	o	o
3. To approve an amendment to our 2012 Plan to increase the number of shares of Common Stock authorized thereunder from 600,000 to 1,000,000, and to increase the number of shares available for new grants thereunder to our	o	o	o

employees, officers and directors from 185,346 to 585,346.

4. To ratify the selection of EisnerAmper LLP as the Company s independent registered public accounting firm for the fiscal year ending December 31, 2018 o o o

THIS PROXY, WHEN PROPERLY EXECUTED, WILL BE VOTED IN THE MANNER DIRECTED HEREIN BY THE UNDERSIGNED STOCKHOLDER. IF NO DIRECTION IS MADE, THIS PROXY WILL BE VOTED FOR EACH OF THE NOMINEES IN ITEM 1 AND FOR PROPOSAL 2, 3, AND 4, AND AS THE PROXIES DEEM ADVISABLE ON SUCH OTHER MATTERS AS MAY PROPERLY COME BEFORE THE MEETING.

Please sign exactly as the name appears below. When shares are held by joint tenants, both should sign. When signing as attorney, as executor, administrator, trustee or guardian, please give full title as such. If a corporation, please sign in full corporate name by President or other authorized officer, giving full title as such. If a partnership, please sign in partnership name by authorized person.

I will o will not o attend the Meeting

Dated: , 2018

SIGNATURE

SIGNATURE IF HELD JOINTLY

PLEASE MARK, SIGN, DATE AND RETURN THE PROXY CARD PROMPTLY USING THE ENCLOSED ENVELOPE THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS OF WAYSIDE TECHNOLOGY GROUP, INC.