IMPERVA INC
Form 10-Q
August 08, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended June 30, 2014

OR

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

For the Transition Period from __________ to __________

Commission File Number 001-35338

Imperva, Inc.

(Exact name of the Registrant as Specified in its Charter)

Delaware	**03-0460133**
(State or Other Jurisdiction of	**(I.R.S. Employer**
Incorporation or Organization)	**Identification No.)**

3400 Bridge Parkway, Suite 200

Redwood Shores, California 94065

(Address of Principal Executive Offices, including Zip Code)

(650) 345-9000

(Registrant s Telephone Number, including Area Code)

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

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

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

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

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

Shares of Imperva, Inc. common stock, $0.0001 par value per share, outstanding as of August 1, 2014: 26,494,702 shares.

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IMPERVA, INC.

FORM 10-Q

Quarterly Period Ended June 30, 2014

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

IMPERVA, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(In thousands, except share and per share data)

	June 30, 2014 Unaudited	December 31, 2013 *
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 62,990	$ 76,704
Short-term investments	36,489	38,381
Restricted cash	57	34
Accounts receivable, net of allowance for doubtful accounts of $592 and $410 as of June 30, 2014 and December 31, 2013, respectively	33,604	44,446
Inventory	324	512
Deferred tax assets	374	341
Prepaid expenses and other current assets	3,398	3,972
Total current assets	137,236	164,390
Property and equipment, net	6,732	5,475
Goodwill	34,972	
Acquired intangible assets, net	10,103	
Severance pay fund	4,599	4,140
Restricted cash	1,575	1,252
Deferred tax assets	42	42
Other assets	719	1,192
TOTAL ASSETS	$ 195,978	$ 176,491
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 3,298	$ 3,948
Accrued compensation and benefits	12,235	12,930
Accrued and other current liabilities	4,369	3,961
Deferred revenue	42,206	40,337
Total current liabilities	62,108	61,176
Other liabilities	10,129	1,993
Deferred revenue	21,936	22,715
Accrued severance pay	5,078	4,385

TOTAL LIABILITIES	99,251	90,269
Commitments and Contingencies (Note 9)		
STOCKHOLDERS EQUITY:		
Preferred stock, $0.0001 par value - 5,000,000 shares authorized, no shares issued and outstanding as of June 30, 2014 and December 31, 2013		
Common stock, $0.0001 par value - 145,000,000 shares authorized, 26,508,022 and 25,206,498 shares issued and outstanding as of June 30, 2014 and December 31, 2013, respectively	2	2
Additional paid-in capital	228,602	187,957
Accumulated deficit	(131,544)	(98,695)
Accumulated other comprehensive loss	(333)	(428)
TOTAL IMPERVA, INC. STOCKHOLDERS EQUITY	96,727	88,836
Noncontrolling interest		(2,614)
TOTAL STOCKHOLDERS EQUITY	96,727	86,222
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 195,978	$ 176,491

(*) The Condensed Consolidated Balance Sheet as of December 31, 2013 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

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

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IMPERVA, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Operations

(In thousands, except per share data)

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2014	**2013**	**2014**	**2013**
Net revenue:				
Products and license	$ 16,586	$ 15,671	$ 28,557	$ 29,825
Services	21,856	15,668	41,401	30,099
Total net revenue	38,442	31,339	69,958	59,924
Cost of revenue:				
Products and license	2,075	2,446	3,807	4,322
Services	6,959	5,098	12,979	9,513
Total cost of revenue	9,034	7,544	16,786	13,835
Gross profit	29,408	23,795	53,172	46,089
Operating expenses:				
Research and development	11,618	6,646	21,579	13,004
Sales and marketing	25,065	18,281	48,100	35,828
General and administrative	7,621	4,597	16,026	8,980
Amortization of acquired intangible assets	362		566	
Total operating expenses	44,666	29,524	86,271	57,812
Loss from operations	(15,258)	(5,729)	(33,099)	(11,723)
Other income (expense), net	(215)	(55)	(369)	(102)
Loss before provision (benefit) for income taxes	(15,473)	(5,784)	(33,468)	(11,825)
Provision (benefit) for income taxes	(35)	261	(406)	415
Net loss	(15,438)	(6,045)	(33,062)	(12,240)
Loss attributable to noncontrolling interest		130	213	266
Net loss attributable to Imperva, Inc. stockholders	$ (15,438)	$ (5,915)	$ (32,849)	$ (11,974)
Net loss per share of common stock attributable to Imperva, Inc. stockholders, basic and diluted	$ (0.60)	$ (0.24)	$ (1.29)	$ (0.50)

Shares used in computing net loss per share of common stock, basic and diluted	25,782	24,171	25,545	24,039

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

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IMPERVA, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Comprehensive Loss

(in thousands)

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2014	**2013**	**2014**	**2013**
Net loss	$ (15,438)	$ (6,045)	$ (33,062)	$ (12,240)
Other comprehensive loss (net of tax):				
Net change in net unrealized gain (loss) on investments	11	(141)	14	(208)
Net change in unrealized gain (loss) on hedging instruments	81	(234)	81	(97)
	92	(375)	95	(305)
Comprehensive loss	(15,346)	(6,420)	(32,967)	(12,545)
Comprehensive loss attributable to noncontrolling interest		130	213	266
Comprehensive loss attributable to Imperva, Inc. stockholders	$ (15,346)	$ (6,290)	$ (32,754)	$ (12,279)

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

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IMPERVA, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Stockholders Equity

(In thousands, except share data)

(Unaudited)

	Common Stock Shares	Amount	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interest	Total Stockholders Equity
For the six months ended June 30, 2014							
Balance as of January 1, 2014	25,206,498	$ 2	$ 187,957	$ (98,695)	$ (428)	$ (2,614)	$ 86,222
Issuance of common stock related to acquisitions	738,479		24,164				24,164
Issuance of common stock, net of repurchases	473,442		3,223				3,223
Vesting of restricted stock			400				400
Stock-based compensation			15,331				15,331
Pre-combination service relating to acquired Skyfence option plan			354				354
Purchase of noncontrolling interest in Incapsula	89,603		(2,827)			2,827	
Components of other comprehensive income (loss), net of tax:							
Change in unrealized gain (loss) on investments					14		14
Change in unrealized gain (loss) on derivatives					81		81
Net loss				(32,849)		(213)	(33,062)
Comprehensive loss							(32,967)
	26,508,022	$ 2	$ 228,602	$ (131,544)	$ (333)	$	$ 96,727

Balance as of June 30, 2014

	Common Stock		Additional Paid-In	Accumulated	Accumulated Other Comprehensive Income (Loss)	Noncontrolling	Total Stockholders
	Shares	Amount	Capital	Deficit		Interest	Equity
For the six months ended June 30, 2013							
Balance as of January 1, 2013	24,296,076	$ 2	$ 157,989	$ (73,517)	$ 861	$ (1,104)	$ 84,231
Issuance of common stock, net of repurchases	448,410		2,893				2,893
Vesting of restricted stock			400				400
Stock-based compensation			6,445				6,445
Sale of additional ownership in Incapsula			37			(37)	
Components of other comprehensive income (loss), net of tax:							
Change in unrealized gain (loss) on investments					(208)		(208)
Change in unrealized gain (loss) on derivatives					(97)		(97)
Net loss				(11,974)		(266)	(12,240)
Comprehensive loss							(12,545)
Balance as of June 30, 2013	24,744,486	$ 2	$ 167,764	$ (85,491)	$ 556	$ (1,407)	$ 81,424

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

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IMPERVA, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Six months ended June 30,	
	2014	**2013**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (33,062)	$ (12,240)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,688	1,269
Stock-based compensation	15,331	6,445
Amortization of acquired intangibles	566	
Amortization of premiums/accretion of discounts on short-term investments	217	383
Changes in operating assets and liabilities:		
Accounts receivable, net	10,842	8,489
Inventory	188	(40)
Prepaid expenses and other assets	1,207	(404)
Accounts payable	(928)	(16)
Accrued compensation and benefits	(884)	1,350
Accrued and other liabilities	(88)	(390)
Severance pay (net)	234	65
Deferred revenue	1,090	2,012
Deferred tax assets	(33)	(18)
Other	(1)	(8)
Net cash provided by (used in) operating activities	(3,633)	6,897
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of short-term investments	(11,615)	(27,026)
Proceeds from sales/maturities of short-term investments	13,585	29,361
Acquisitions, net of cash acquired	(12,083)	
Purchase of property and equipment	(2,845)	(1,202)
Change in restricted cash	(346)	59
Net cash provided by (used in) investing activities	(13,304)	1,192
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock, net of repurchases	3,223	2,893
Net cash provided by financing activities	3,223	2,893
Effect of exchange rate changes on cash and cash equivalents		(162)

NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		(13,714)		10,820
CASH AND CASH EQUIVALENTS - Beginning of period		76,704		59,201
CASH AND CASH EQUIVALENTS - End of period	$	62,990	$	70,021
NONCASH INVESTING AND FINANCING ACTIVITIES:				
Vesting of restricted and early exercised stock options	$	400	$	400
Common stock issued in connection with acquisitions	$	24,164	$	

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

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IMPERVA, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of Presentation and Summary of Significant Accounting Policies

Business

Imperva, Inc. (together with its subsidiaries, the Company or we) was incorporated in April 2002 in Delaware. The Company is headquartered in Redwood Shores, California and has subsidiaries located throughout the world including Israel, Asia and Europe. The Company is engaged in the development, marketing, sales, service and support of data center security solutions that protect high value applications and data assets in physical and virtual data centers.

Basis of Presentation

The Company has prepared the accompanying unaudited Condensed Consolidated Financial Statements in accordance with Article 10 of Regulation S-X and pursuant to the rules and regulations for Form 10-Q of the Securities and Exchange Commission (the SEC). Pursuant to those rules and regulations, the Company has condensed or omitted certain information and footnote disclosure it normally includes in its annual consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP). In management s opinion, the Company has made all adjustments (consisting only of normal, recurring adjustments, except as otherwise indicated) necessary to fairly present its consolidated financial position, results of operations, and cash flows. The Company s interim period operating results do not necessarily indicate the results that may be expected for any other interim period or for the full fiscal year. These financial statements and accompanying notes should be read in conjunction with the consolidated financial statements and notes thereto in the Company s Annual Report on Form 10-K for the year ended December 31, 2013, which was filed with the SEC on February 28, 2014 (the Annual Report).

During the three months ended March 31, 2014, we revised our business segments based upon the acquisition of the remaining shares of Incapsula, Inc. that the Company did not already own. As a result, we no longer separately report the Incapsula segment and the Company now operates in one operating, and therefore, reportable segment in order to better align Incapsula with our strategic approach to the markets and customers we serve. The reclassification of historical business segment information had no impact on the Company s basic financial statements.

Basis of Consolidation

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned and majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. On March 20, 2014, the Company acquired the remaining interest it did not previously own in its majority-owned subsidiary, Incapsula, Inc. (Incapsula) (Refer to Note 2). The Company separately presented the non-controlling interest on its Condensed Consolidated Balance Sheets in Total Stockholder s Equity and in its Condensed Consolidated Statements of Operations for periods prior to such date.

Goodwill and Acquired Intangibles

Goodwill represents the excess of the aggregate purchase price paid over the fair value of the net tangible assets acquired. Goodwill is not amortized and is reviewed at least annually or whenever events or changes in circumstances

indicate that the carrying value may not be recoverable. In reviewing goodwill, the Company performs a qualitative assessment to test the reporting unit s goodwill for impairment. Based on the Company s qualitative assessment, if we determine that the fair value of the reporting unit is more likely than not (i.e. a likelihood of more than 50 percent) to be less than the carrying amount, the two step impairment test will be performed. The first step of the impairment test involves comparing the fair value of the reporting unit to its net book value, including goodwill. If the net book value exceeds its fair value, then the Company would perform the second step of the goodwill impairment test to determine the amount of the impairment loss. The impairment loss would be calculated by comparing the implied fair value of the Company to its net book value. In calculating the implied fair value of the Company s goodwill, the fair value of the Company would be allocated to all of the other assets and liabilities based on their fair values. The excess of the fair value of the Company over the amount assigned to its other assets and liabilities is the implied fair value of goodwill. An impairment loss would be recognized when the carrying amount of goodwill exceeds its implied fair value.

The Company completes its annual impairment test during the fourth quarter of each fiscal year. There was no impairment of goodwill recorded for the six months ended June 30, 2014.

We amortize intangible assets with finite lives over their estimated useful lives and review them for impairment whenever an impairment indicator exists. We continually monitor events and changes in circumstances that could indicate carrying amounts of our intangible assets may not be recoverable. When such events or changes in circumstances occur, we assess recoverability by determining whether the carrying value of such assets will be recovered through the undiscounted expected future cash flows. If the future undiscounted cash flows are less than the carrying amount of these assets, we recognize an impairment loss based on any excess of the carrying amount over the fair value of the assets. We did not recognize any intangible asset impairment charges in the six months ended June 30, 2014. Our intangible assets are amortized over their estimated useful lives of 7 to 10 years. Amortization is based on a straight-line basis as the consumption pattern of the asset is not apparent. The weighted average useful life of our acquired technology intangible assets was 8 years.

Concentration of Revenue and Accounts Receivable

For the three months ended June 30, 2013, the Company had one customer that represented 11% of the Company s total revenue. For the three months ended June 30, 2014 and for the six months ended June 30, 2014 and 2013, the Company did not have any customers that represented more than 10% of the Company s total revenue. There were no customers who represented greater than 10% of gross accounts receivable as of June 30, 2014 or December 31, 2013.

Significant Accounting Policies

Other than the change to our reporting segments and the addition of the Company s policy for accounting for goodwill and acquired intangibles, there have been no material changes to the Company s significant accounting policies as compared to the significant accounting policies described in the Company s Annual Report on Form 10-K for the year ended December 31, 2013.

Recent Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-08, Reporting Discontinued Operations and Disposals of Components of an Entity, which changes the criteria for determining which disposals can be presented as discontinued operations and modifies related disclosure requirements. The new guidance is effective for annual and interim periods beginning after December 15, 2014, with early adoption permitted. The new guidance will be applicable for disposal transactions, if any, that we initiate after the adoption date. The adoption of this guidance is not expected to have a material impact on our financial position, results of operations or cash flows.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, to clarify the principles used to recognize revenue for all entities. The new guidance is effective for annual and interim periods beginning after December 15, 2016 with no early adoption permitted and allows for both retrospective and prospective methods of adoption. We are currently evaluating the impact, if any, the adoption of this guidance will have on our financial position, results of operations or cash flows.

2. Incapsula

On November 5, 2009, the Company entered into a license agreement for Incapsula to use certain developed technology of the Company. In lieu of any other fee or royalty under the license agreement, Incapsula issued to the Company 5,000,000 shares of its Series A Convertible Preferred Stock representing a 58% ownership interest at the date of issuance. The transaction was accounted for as a business combination. No value was assigned to the license on the acquisition date as the use of the license will stay within the control of the Company. Therefore, the Company s

historical carrying value of the developed technology immediately prior to the acquisition was used to determine the value of the purchase consideration exchanged in the transaction. As Incapsula was a newly-formed entity with no net assets on the acquisition date and the value of the license was determined to be zero, no goodwill was recorded by the Company on the acquisition.

On March 9, 2010, the Company entered into a Series A and Series A-1 Purchase Agreement whereby Incapsula issued 6,666,666 shares of its Series A Convertible Preferred Stock to the Company in exchange for cash consideration of $3.0 million. As a result of this transaction, the Company increased its ownership interest in Incapsula to 76% at the date of issuance. The purchase of the additional ownership interest in Incapsula was treated as an equity transaction. Under the terms of the Series A and Series A-1 Purchase Agreement, the Company entered into a forward contract with Incapsula to purchase 8,750,000 shares of Incapsula s Series A-1 Convertible Preferred Stock in exchange for $7.0 million in cash consideration if certain milestones were achieved no later than September 2011. On the transaction date, no value was assigned to the forward contract as the option did not meet the definition of a derivative instrument as it did not contain a net settlement feature. Specifically, the forward contract could only be gross physically settled as Incapsula is a non-publicly traded company whose stock was not readily convertible to cash.

In July 2011, Incapsula achieved the respective performance milestones. As a result, the Company purchased 4,375,000 shares of Incapsula s Series A-1 Preferred Stock for $3.5 million thereby increasing its ownership interest to 82%. In January 2012, the Company purchased the remaining 4,375,000 shares of Incapsula s Series A-1 Preferred Stock for $3.5 million thereby increasing its ownership interest in Incapsula to 85%.

Under the terms of the agreements between the Company and Incapsula, the Company had the right, but not the obligation, to purchase the remaining ownership interest in Incapsula commencing on November 5, 2013 and ending on November 5, 2018 (the Purchase Right). Exercise of the Purchase Right was solely within the Company s control and the price for the remaining ownership interest was to be based on an Incapsula enterprise valuation calculated as the greater of (i) eight times Incapsula s prior 12 months trailing revenues or (ii) seven times the aggregate amount Incapsula had raised in connection with its Series A Convertible Preferred Stock financings. On the acquisition date, no value was assigned to this Purchase Right as the option does not meet the definition of a derivative instrument as it does not contain a net settlement feature. Specifically, the Purchase Right could only be gross physically settled as Incapsula was a non-publicly traded company whose stock was not readily convertible to cash.

In March 2010, the board of directors of Incapsula adopted the Incapsula 2010 Share Incentive Plan pursuant to which Incapsula may grant to its employees options to purchase shares of Incapsula s common stock or restricted shares. Pursuant to the Purchase Right option discussed above, awards under the Incapsula 2010 Share Incentive Plan would be assumed by the Company, substituted with Company stock options or cashed out, and all outstanding awards and the Incapsula 2010 Share Plan would terminate.

In March 2014, the Company acquired the remaining outstanding capital stock in exchange for approximately 124,088 shares of Company common stock with an aggregate fair value of $7.7 million, of which 34,485 shares are subject to a 15-month holdback pursuant to the acquisition agreement, and assumed outstanding options to acquire capital stock of Incapsula not already owned by Imperva (the Incapsula Acquisition) which are equivalent to 48,359 shares of Company common stock on an as-converted basis. The aggregate consideration for the Incapsula Acquisition is substantially on the same terms of the Purchase Right less the outstanding principal and interest under the Incapsula Loan. In addition, during 2013, the Company issued RSUs for approximately 264,878 shares of Imperva common stock with performance-based vesting tied to 2014 revenue for Incapsula and Incapsula-related products and services (effectively valuing such revenues similarly to the Purchase Right) less the outstanding principal and interest under the Incapsula Loan. At the same time, Incapsula issued similar RSUs for approximately 198,825 shares on an as-converted to Imperva common stock-basis, which the Company assumed in connection with the Incapsula Acquisition, in addition to the consideration for the Incapsula Purchase. These performance-based RSUs granted by Imperva and Incapsula were issued to continuing employees of Incapsula.

As of the date of the acquisition, the remaining non-controlling interest on the Company s balance sheet of $2.8 million was reclassified to additional paid-in capital given the Company s complete ownership of Incapsula.

3. Acquisitions

Acquisitions during the first six months of 2014 were accounted for in accordance with Accounting Standards Codification (ASC) No. 805, *Business Combinations*, and the results of operations of each acquisition have been included in our consolidated results of operations from the respective date of the acquisition. Each of the acquisitions was not material, either individually or in the aggregate to our results of operations in the period of acquisition.

While we use our best estimates and assumptions as part of the purchase price allocation process to value assets acquired and liabilities assumed at the business combination date, our estimates and assumptions are subject to refinement. As a result, during the preliminary purchase price allocation period, which may be up to one year from the business combination date, we record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. We record adjustments to assets acquired or liabilities assumed subsequent to the purchase price allocation period in our operating results in the period in which the adjustments were determined.

The total purchase price allocated to the tangible assets acquired is assigned based on the fair values as of the date of the acquisition. The fair value assigned to identifiable intangible assets acquired is determined using the income approach which discounts expected future cash flows to present value using estimated assumptions determined by management. We believe that these identified intangible assets will have no residual value after their estimated economic useful lives. The identifiable intangible assets are subject to amortization on a straight-line basis as this best approximates the benefit period related to these assets.

The excess of the purchase price over the identified tangible and intangible assets, less liabilities assumed, is recorded as goodwill and primarily reflects the value of the synergies expected to be generated from combining our and the acquired entities technology and operations.

Acquisition of Skyfence Networks Ltd.

On February 7, 2014, the Company acquired Skyfence Networks Ltd. (Skyfence), a private company based and incorporated in Israel. Skyfence is a developer of a solution which allows real time visibility and control over corporate use of software-as-a-Service (SaaS) applications, which enforces security policy, protects sensitive data from external and inside threats, as well as ensures compliance with standards.

Per the terms of the acquisition agreement (as amended) with Skyfence and its security holders, we purchased all of the outstanding shares of capital stock of Skyfence in exchange for (a) approximately $8.6 million in cash, in addition to a holdback payment commitment due 24 months from the acquisition close valued at approximately $7.2 million, and (b) 884,422 shares of Company common stock, of which 532,262 shares are subject to forfeiture based upon time-based vesting and continuing employment, and were therefore excluded from purchase consideration as such amounts will be recorded as compensation expense over the term of the corresponding four-year service period. In addition, 29,871 of the shares are subject to a holdback period of up to 24 months from the date of acquisition. We also assumed stock options outstanding in accordance with the terms of the applicable Skyfence stock option plan and Skyfence stock option agreement relating to that Skyfence stock option. Based on Skyfence s stock options outstanding at February 7, 2014, Imperva converted options to purchase 164,000 shares of Skyfence stock into options to purchase 24,828 shares of Imperva common stock.

The fair value of Imperva s shares issued is based on Imperva s closing price per share of $59.08 as reported on the New York Stock Exchange at the closing of the Acquisition on February 7, 2014.

The fair values of the stock option awards assumed were estimated using a Black-Scholes option-pricing model. The estimated fair values of unvested equity awards of $1.1 million will be recorded as operating expense over the remaining requisite service periods as they relate to post-combination services, while the fair values of vested equity based awards of $0.3 million were included in total purchase price as they relate to pre-combination services. The total purchase consideration is as follows (in thousands):

Cash	$ 8,558
Cash holdback liability	7,157
Fair value of common stock	20,855
Estimated fair value of equity awards assumed and replaced	354
	$ 36,924

The acquisition of Skyfence was accounted for in accordance with the acquisition method of accounting for business combinations with Imperva as the accounting acquirer. We expensed the related acquisition costs in the amount of $0.9 million in general and administrative expenses. In addition, stock-based compensation expense totaling $3.2 million was recognized from the date of acquisition through June 30, 2014.

The excess of the consideration for SkyFence over the fair values assigned to the assets acquired and liabilities assumed represents the goodwill resulting from the acquisition. Management believes that the goodwill represents the synergies expected from combining the products and technologies of Imperva with those of Skyfence, which will enhance the Company s overall product portfolio. The purchased technology will be amortized straight-line over a seven-year preliminary estimated useful life. Also as part of the acquisition, we assumed deferred tax liabilities related to the fair value of the developed technology we obtained in the acquisition. Goodwill recorded in connection with the acquisition is not deductible for income tax purposes. The total purchase price was allocated using the information available at the business combination date. The following table summarizes the allocation of the consideration to the fair value of the tangible and intangible assets acquired and liabilities assumed as of the acquisition date (table in thousands):

Net tangible assets	$ 1,014
Existing technology	7,965
Deferred tax liability assumed	(1,528)
Goodwill	29,473
Total purchase price	$ 36,924

The results of operations of Skyfence described above have been included in Imperva s consolidated financial statements from the date of acquisition. The following table presents pro forma results of operations of the Company and Skyfence as if the companies had been combined as of January 1, 2013, and includes pro forma adjustments related to the amortization of acquired intangible assets and share-based compensation expense and the related income tax effects. Direct transaction costs are excluded from the June 30, 2014 pro forma condensed combined financial information presented below. For pro forma purposes, during the six months ended June 30, 2014 and 2013, $148,000 and $248,000, respectively, of income tax benefit associated with the deferred tax liability was recognized in earnings. The pro forma condensed combined financial information is presented for informational purposes only. The unaudited pro forma results of operations are not necessarily indicative of results that would have occurred had the acquisition taken place at the beginning of the earliest period presented, or of future results. Included in the pro forma results are fair value adjustments based on the fair values of assets acquired and liabilities assumed as of the acquisition date. Supplemental information on an unaudited pro forma basis, as if the Skyfence acquisition had been consummated on January 1, 2013 is presented as follows (in thousands):

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	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Pro forma revenue	$ 38,442	$ 31,339	$ 69,958	$ 59,924
Pro forma loss from operations	$ (15,259)	$ (8,529)	$ (33,868)	$ (17,324)
Pro forma net loss	$ (15,548)	$ (8,695)	$ (33,684)	$ (17,540)

Acquisition of Certain Assets and Liabilities of Tomium Software, LLC.

On January 30, 2014, the Company acquired certain assets and liabilities of Tomium Software, LLC (Tomium), a private company based in Texas. Tomium is a provider of real-time mainframe security auditing agents. The purchase price of approximately $8.3 million includes approximately $4.6 million in cash and assumption of a liability to pay cash of $0.3 million, and also the issuance of 60,556 shares of Company common stock valued at approximately $3.4 million based upon the closing price of the Company s stock on the acquisition date of $55.45 per share. Imperva acquired certain tangible assets and also assumed a facility lease of Tomium.

The following table summarizes the preliminary allocation of the consideration to the fair value of the tangible and intangible assets acquired and liabilities assumed as of the acquisition date based on information available at the business combination date (amounts in table in thousands):

Intangible assets	$ 2,704
Goodwill	5,499
Total intangible assets acquired	8,203
Other acquired tangible assets	60
Fair value of assets acquired	$ 8,263

The total purchase price was allocated using the information available at the business combination date. Goodwill recorded in connection with the acquisition is deductible for U.S. income tax purposes.

The acquisition of Tomium was accounted for in accordance with the acquisition method of accounting for business combinations with Imperva as the accounting acquirer. We expensed the related acquisition costs, consisting primarily of legal costs in the amount of $0.3 million in general and administrative expenses. Management believes that the goodwill represents the synergies expected from combining the acquired technology and operations with those of Imperva. The intangible assets acquired by Imperva in conjunction with the acquisition of Tomium are being amortized straight-line over a ten-year estimated useful life.

The results of operations related to the Tomium assets and liabilities have been included in our consolidated statements of operations from the acquisition date. Pro forma results of operations have not been presented because the acquisition was not material to the Company s results of operations.

4. Cash, Cash Equivalents, and Short-Term Investments

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. Cash and cash equivalents consist of cash on hand, highly liquid investments in commercial paper, money market funds and various deposit accounts.

The Company considers all high quality investments purchased with original maturities at the date of purchase greater than three months to be short-term investments. Investments are available to be used for current operations and are, therefore, classified as current assets even though maturities may extend beyond one year. Cash equivalents and short-term investments are classified as available-for-sale and are, therefore, recorded at fair value on the condensed consolidated balance sheets, with any unrealized gains and losses reported in accumulated other comprehensive income (loss), which is reflected as a separate component of stockholders equity in its condensed consolidated balance sheets, until realized. The Company uses the specific-identification method to compute gains and losses on the investments. The amortized cost of securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization and accretion is included as a component of other income (expense), net in the condensed consolidated statements of operations.

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Cash, cash equivalents and short-term investments consist of the following (in thousands):

	As of June 30, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash and cash equivalents:				
Cash	$ 25,306	$	$	$ 25,306
Commercial paper	23,988		1	23,987
Bank deposits	11,009			11,009
Money market funds	2,688			2,688
Total	$ 62,991	$	$ 1	$ 62,990
Short-term investments:				
Corporate debt obligations	$ 26,211	$ 35	$ 1	$ 26,245
Bank deposits	10,244			10,244
Total	$ 36,455	$ 35	$ 1	$ 36,489

	As of December 31, 2013			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash and cash equivalents:				
Cash	$ 41,973	$	$	$ 41,973
Commercial paper	21,948		1	21,947
Bank deposits	10,165			10,165
Money market funds	2,619			2,619
Total	$ 76,705	$	$ 1	$ 76,704
Short-term investments:				
Corporate debt obligations	$ 28,220	$ 22	$ 14	$ 28,228
Bank deposits	10,153			10,153
Total	$ 38,373	$ 22	$ 14	$ 38,381

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The following table summarizes the cost and estimated fair value of short-term investments based on stated effective maturities as of June 30, 2014 (in thousands):

	As of June 30, 2014	
	Amortized Cost	Estimated Fair Value
Short-term investments:		
Due within one year	$ 25,352	$ 25,374
Due within two years	11,103	11,115
Total	$ 36,455	$ 36,489

The Company reviews its short-term investments on a regular basis to evaluate whether or not any security has experienced an other-than-temporary decline in fair value. The Company considers factors such as the length of time and extent to which the market value has been less than the cost, the financial condition and near-term prospects of the issuer and its intent to sell, or whether it is more likely than not the Company will be required to sell, the investment before recovery of the investment s amortized cost basis. If the Company believes that an other-than-temporary decline exists in one of these securities, the Company writes down these investments to fair value. For debt securities, the portion of the write-down related to credit loss would be recorded to other income (expense), net, in the Company s condensed consolidated statements of operations. Any portion not related to credit loss would be recorded to accumulated other comprehensive income (loss), which is reflected as a separate component of stockholders equity in the Company s condensed consolidated balance sheets. During the six months ended June 30, 2014, the Company did not consider any of its investments to be other-than-temporarily impaired.

None of the Company s short-term investments have been in an unrealized loss position for more than twelve months as of June 30, 2014 and December 31, 2013.

5. Fair Value of Financial Instruments

The Company evaluates assets and liabilities subject to fair value measurements on a recurring basis to determine the appropriate level to classify them for each reporting period. There have been no transfers between fair value measurement levels during the six months ended June 30, 2014.

The Company s cash equivalents and short-term investment instruments are classified within Level 1 or Level 2 of the fair value hierarchy because they are valued using quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency. The types of instruments valued based on quoted market prices in active markets include mutual funds and money market securities, and are generally classified within Level 1 of the fair value hierarchy. The types of instruments valued based on quoted prices in less active markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability include U.S. agency securities, investment-grade corporate bonds, bank deposits, and commercial paper. Such instruments are generally classified within Level 2 of the fair value hierarchy.

The Company executes its foreign currency contracts primarily in the retail market in an over-the-counter environment with a relatively high level of price transparency. The market participants usually are large multi-national and regional banks. The Company s foreign currency contracts valuation inputs are based on quoted prices and quoted

pricing intervals from public data sources and do not involve management judgment. These contracts are typically classified within Level 2 of the fair value hierarchy.

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The following table sets forth the Company s assets and liabilities that were measured at fair value as of June 30, 2014 and December 31, 2013, by level within the fair value hierarchy (in thousands):

	As of June 30, 2014			
	Level I	Level II	Level III	Fair Value
Financial Assets:				
Cash and cash equivalents:				
Commercial paper	$	$ 23,987	$	$ 23,987
Bank deposits		11,009		11,009
Money market funds	2,688			2,688
Short-term investments:				
Corporate debt obligations		26,245		26,245
Bank deposits		10,244		10,244
Total financial assets	$ 2,688	$ 71,485	$	$ 74,173
Prepaid expenses and other current assets - Forward foreign exchange contracts	$	$ 128	$	$ 128

	As of December 31, 2013			
	Level I	Level II	Level III	Fair Value
Financial Assets:				
Cash and cash equivalents:				
Commercial paper	$	$ 21,947	$	$ 21,947
Bank deposits		10,165		10,165
Money market funds	2,619			2,619
Short-term investments:				
Corporate debt obligations		28,228		28,228
Bank deposits		10,153		10,153
Total financial assets	$ 2,619	$ 70,493	$	$ 73,112

In addition to the amounts disclosed in the above table, the fair value of the Company s Israeli severance pay assets, which were comprised of Level II assets, was $4.6 million and $4.1 million as of June 30, 2014 and December 31, 2013, respectively.

6. Derivative Instruments

The Company s primary objective for holding derivative instruments is to reduce its exposure to foreign currency rate changes. The Company reduces its exposure by entering into forward foreign exchange contracts with respect to operating expenses that are forecast to be incurred in currencies other than U.S. dollars. Substantially all of the Company s revenue and capital purchasing activities and a majority of its operating expenditures are transacted in U.S. dollars. However, certain operating expenditures are incurred in or exposed to other currencies, primarily the Israeli

shekel and the Euro.

The Company has established forecasted transaction currency risk management programs to protect against fluctuations in fair value and the volatility of future cash flows caused by changes in exchange rates. The Company s currency risk management program includes forward foreign exchange contracts designated as cash flow hedges. These forward foreign exchange contracts generally mature within 12 months. The Company does not enter into derivative financial instruments for trading purposes.

There were no outstanding derivative instruments as of December 31, 2013. Derivative instruments measured at fair value and their classification on the condensed consolidated balance sheet as of June 30, 2014 is presented in the following table (in thousands):

	Asset as of June 30, 2014 (unaudited)	
	Notional Amount	**Fair Value**
Foreign Exchange Forward Contract Derivatives in cash flow hedging relationships - included in prepaid expenses and other current assets	$ 14,109	$ 128

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Gains (losses) on derivative instruments and their classification on the condensed consolidated statement of operations are presented in the following table (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Foreign Exchange Forward Contract Derivatives in cash flow hedging relationships:				
Gains recognized in OCI (a)	$ 132	$ 59	$ 132	$ 486
Losses recognized in OCI (a)	(14)		(14)	
Gains reclassified from accumulated OCI into net loss (b)	4	360	4	583
Losses reclassified from accumulated OCI into net loss (b)	(14)		(14)	
Foreign Exchange Forward Contract Derivatives not designated as hedging relationships:				
Gains recognized in net loss (c)	$	$ 25	$	$ 27
Losses recognized in net loss (c)				(57)

(a) Net change in the fair value of the effective portion classified in other comprehensive income (loss) (OCI).
(b) Effective portion of cash flow hedges reclassified from accumulated other comprehensive income (loss) into net loss, of which $(1) and $(9) were recognized within cost of sales and operating expenses, respectively, for the three months ended June 30, 2014 and $(1) and $(9) were recognized within cost of sales and operating expenses, respectively, for the six months ended June 30, 2014. $22 and $338 were recognized within cost of sales and operating expenses, respectively for the three months ended June 30, 2013 and $39 and $544 were recognized within cost of sales and operating expenses, respectively, for the six months ended June 30, 2013. All amounts are reflected within the respective condensed consolidated statement of operations.
(c) Classified in other income (expense), net.

7. Acquired Intangible Assets

Acquired technology intangible assets subject to amortization as of June 30, 2014 were as follows (in thousands):

	Cost	Accumulated Amortization	Net
Acquired Technology	$ 10,669	$ (566)	$ 10,103

Acquired intangible assets are amortized over their estimated useful lives of 7 to 10 years. There were no acquired intangible assets prior to January 1, 2014. As of June 30, 2014, we expect amortization expense in future periods to be as follows (in thousands):

	Acquired Technology
Fiscal Year	

2014	$	704
2015		1,408
2016		1,408
2017		1,408
2018		1,408
Thereafter		3,767
Total Expected Amortization Expense	$	10,103

8. Revolving Credit Facility

In September 2010, the Company entered into a revolving credit facility with a financial institution. The agreement, as amended, provides for a maximum borrowing capacity of up to $6.0 million as of June 30, 2014. As of June 30, 2014 and December 31, 2013, there was no balance outstanding on the credit facility.

The credit facility expires on May 1, 2015, is secured by the assets of the Company, and contains a restrictive covenant that requires the Company to maintain a minimum cash and cash equivalents balance of $3.0 million. The terms of this agreement requires payment of an unused line fee of 0.25% per quarter of the unused portion and bears interest at LIBOR plus 2.75%. As of June 30, 2014 and December 31, 2013, the Company was compliant with the amended covenant of the credit facility.

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9. Commitments and Contingencies

(a) Operating Leases

The Company rents its facilities under operating leases with lease periods expiring through 2019. Future minimum payments under these facility operating leases and minimum rentals to be received under non-cancellable subleases are as follows as of June 30, 2014 (in thousands):

Year Ending December 31:	Operating Leases	Estimated Sublease Income
2014 (remaining 6 months)	$ 2,922	$ 251
2015	5,761	244
2016	5,731	81
2017	4,973	
2018	3,443	
Thereafter	347	
Total	$ 23,177	$ 576

Rent expense for the Company s operating leases is recognized on a straight-line basis over the lease term. Rent expense for the six months ended June 30, 2014 and 2013 was $1.9 million and $1.7 million, respectively.

In connection with a lease of office space, the Company received tenant improvement allowances of $336,000 and $639,000 during the years ended December 31, 2012 and 2010, respectively, from the lessor for certain improvements made to the leased property. The Company has recorded the tenant improvement allowances as a leasehold improvement within property and equipment, net, and as deferred rent within other liabilities on the condensed consolidated balance sheets. The deferred rent liability is amortized to rent expense over the term of the lease on a straight-line basis. The leasehold improvements are being amortized to expense over the period from when the improvements were placed into service until the end of their useful life, which is the end of the lease term.

In addition, certain of the Company s operating lease agreements for office space also include rent holidays and scheduled rent escalations during the initial lease term. The Company has recorded the rent holidays as a deferred rent within other liabilities on the condensed consolidated balance sheets. The Company recognizes the deferred rent liability and scheduled rent increase on a straight-line basis into rent expense over the lease term commencing on the date the Company takes possession of the lease space.

As of June 30, 2014 the Company has $1.6 million in restricted deposits to secure bank guarantees provided to its lessors.

(b) Cancelable Lease Agreement

The Company leases motor vehicles under a cancelable operating lease agreement. The Company has an option to cancel the lease agreement, which may result in penalties in a maximum amount of $89,000 as of June 30, 2014. Motor vehicle lease expenses for the six months ended June 30, 2014 and 2013 were $1.4 million and $1.2 million, respectively.

(c) Purchase Commitments

As of June 30, 2014 and December 31, 2013, the Company had purchase commitments of $5.9 million and $3.2 million, respectively, to purchase inventory, trial units, and research and development equipment from its vendors. The purchase commitments result from the Company s contractual obligation to order or build inventory in advance of anticipated sales. According to the Company s agreements with its vendors, the Company committed to purchase inventory within nine months from the date the inventory arrived at the vendor s warehouse.

(d) Litigation

From time to time, the Company may be subject to other legal proceedings and claims in the ordinary course of business.

On April 11, 2014, a purported shareholder class action lawsuit was filed in the United States District Court for the Northern District of California against Imperva and certain of its officers. The lawsuit purports to bring suit on behalf of those investors who purchased Imperva s publicly traded securities between May 2, 2013 and April 9, 2014. Plaintiff alleges that defendants made false and misleading statements, purports to assert claims for violations of the federal securities laws, and seeks unspecified compensatory damages and other relief. A response to the complaint is not yet due.

On June 27, 2014, a purported shareholder derivative lawsuit was filed in the Court of Chancery for the State of Delaware against Imperva (as a nominal defendant), and naming certain officers and members of Imperva s board of directors as individual defendants. The lawsuit relates to the acquisition of SkyFence Networks, Ltd. and the complaint asserts claims for breach of fiduciary duty and unjust enrichment, and seeks to recover unspecified compensatory damages allegedly sustained by Imperva, corporate reforms, the recovery of plaintiffs attorney s fees and other relief. A response to the complaint is not yet due.

In addition, the Company has received, and may in the future continue to receive, claims from third parties asserting, among other things, infringement of intellectual property rights. While the outcome of these matters is remote, the Company does not expect that the ultimate costs to resolve these matters will have a material effect on our consolidated financial position, results of operations or cash flows. The Company will record a liability when it believes that it is both probable that a loss has been incurred and the amount can be reasonably estimated.

(e) Indemnification

Under the indemnification provisions of its standard sales contracts, the Company agrees to defend its channel partners and end customers against third-party claims asserting infringement of certain intellectual property rights, which may include patents, copyrights, trademarks, or trade secrets, and to pay judgments and settlements entered on such claims. The Company s exposure under these indemnifications provisions is generally limited to the total amount paid under the agreement. However, certain agreements included indemnification provisions that could potentially expose the Company to losses in excess of the amount received under the agreement. To date, there have been no claims under such indemnification provisions. Accordingly, the Company has not recorded a liability on its consolidated balance sheets for these indemnification provisions.

In addition to the foregoing, the Company maintains director and officer insurance, which may cover certain liabilities arising from its obligation to indemnify its directors and officers.

10. Stock Plans

(a) 2003 Stock Plan

During 2003, the Board of Directors adopted the 2003 Stock Plan (the 2003 Plan), which allows for the granting of both incentive stock options and non-qualified stock options and the direct award or sale of shares of the Company s common stock (including restricted common stock) to officers, employees, directors, consultants and other key persons. Incentive stock options may be granted to employees with exercise prices of no less than the fair value of the common stock on the grant date, and non-qualified options may be granted to employees, directors, or consultants at exercise prices of no less than 85% of the fair value of the common stock on the grant date, as determined by the Board of Directors. If, at the time the Company grants an option, the optionee directly or by attribution owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company, the option price shall be at least 110% of the fair value. Options granted under the Plan generally expire no later than ten years and, in general, vest four years from the date of grant.

(b) 2011 Stock Option and Incentive Plan

In September 2011, the Board of Directors adopted the 2011 Stock Option and Incentive Plan (the 2011 Plan) which was subsequently approved by the Company s stockholders. The 2011 Plan replaces the 2003 Plan as the Board has decided not to grant any additional awards under that plan. The Company has reserved a total of 1,000,000 shares of common stock for issuance under the 2011 Plan. In addition, any reserved but unissued shares under the 2003 Stock

Plan will be added to the number of shares reserved for issuance under the 2011 Plan. The 2011 Plan also provides that the number of shares reserved and available for issuance under the plan will automatically increase each January 1, beginning in 2012 and ending in 2015, by 4% of the outstanding number of shares of common stock on the immediately preceding December 31. The Board of Directors or compensation committee may reduce the amount of the increase in any particular year. As of December 31, 2013, there were 1,847,752 shares available for grant under the 2011 Plan. On January 1, 2014, the share reserve under the 2011 Plan was automatically increased by 1,008,260 shares.

The 2011 Plan permits the granting of incentive stock options, non-qualified stock options, restricted stock units (RSUs), stock appreciation rights, restricted shares of common stock and performance share awards. The exercise price of stock options may not be less than the 100% of the fair market value of the common stock on the date of grant. Options granted pursuant to the 2011 Plan generally expire in no later than ten years. The Company began granting RSUs in February 2012, which generally vest over either a four-year period with 25% vesting at the end of one year and the remainder vesting quarterly thereafter or they completely vest at the end of a three-year period. Additionally, in conjunction with the Incapsula Acquisition, the Company granted performance-based restricted stock units to an employee of Incapsula for approximately 264,878 shares of Company common stock (Refer to Note 2).

(c) 2011 Employee Stock Purchase Plan

In September 2011, the Board of Directors adopted the 2011 Employee Stock Purchase Plan (the ESPP) which was subsequently approved by the Company s stockholders. The ESPP took effect on the effective date of the registration statement for the Company s IPO. The ESPP permits eligible employees to acquire shares of the Company s common stock by accumulating funds through periodic payroll deductions of up to 15% of base salary. Each offering period may run for no more than 24 months and consist of no more than five purchase periods. The purchase price for shares of the Company s common stock purchased under the ESPP will be 85% of the lesser of the fair market value of the Company s common stock on the first day of the offering period or the last trading day of the applicable purchase period within that offering period.

The Company has initially reserved a total of 500,000 shares of common stock for future issuance under the ESPP. The number of shares reserved for issuance under the ESPP will increase automatically on January 1 of each of the first eight years commencing in 2012 by the number of shares equal to 1% of the Company s total outstanding shares as of the immediately preceding December 31. The Board of Directors or compensation committee may reduce the amount of the increase in any particular year. No more than 20,000,000 shares of common stock may be issued under the ESPP and no other shares may be added to the ESPP without the approval of the Company s stockholders. On January 1, 2014, the share reserve under the 2011 Employee Stock Purchase Plan was automatically increased by 252,065 shares.

(d) Incapsula 2010 Share Incentive Plan

In March 2010, Incapsula s board of directors adopted the Incapsula 2010 Share Incentive Plan (the Incapsula Plan), pursuant to which Incapsula may grant to its employees and service providers options to purchase shares of its common stock, restricted shares, or restricted share units. The total number of shares of common stock that may be granted under the Incapsula Plan shall not exceed 4,733,333 in the aggregate, subject to certain adjustments.

In November 2013, the board of directors of Incapsula approved the grant of restricted stock units for 7,095,461 shares of Incapsula s common stock (Incapsula RSUs). As part of the Incapsula Acquisition, the Incapsula RSUs were assumed and replaced by RSUs for Company Common Stock issued to continuing employees of Incapsula . The Incapsula RSU s vest according to performance-based vesting terms tied to 2014 revenue for Incapsula and Incapsula-related products and services, which were converted into approximately 204,828 shares of Company Common Stock at the same exchange ratio applicable to the Incapsula Acquisition. In addition to performance conditions, the awards are dependent on future market price of Imperva s common stock, which is deemed a market condition under ASC 718.

The following table summarizes option activity under the Incapsula Plan and related information for the six months ended June 30, 2014:

	Shares Available for Grant	Number of Performance-based Restricted Share Units Outstanding	Number of Stock Options Outstanding	Weighted Average Exercise Price
Outstanding - January 1, 2014	89,687	7,095,461	1,806,500	$ 0.47
Granted	(95,000)		95,000	1.25
Exercised	0			
Forfeited	15,213	(12,713)	(2,500)	1.25
Transferred to Imperva 2011 stock option plan	(9,900)	(7,082,748)	(1,899,000)	0.16
Outstanding - June 30, 2014				$

The options outstanding and performance restricted share units under the Incapsula 2010 Share Incentive Plan were assumed as part of the Incapsula Acquisition and are equivalent to 253,187 shares of Company common stock on an as-converted basis. The Company does not intend to grant any additional shares under the Incapsula 2010 Share Incentive Plan.

(e) Stock Compensation Expense

The Company recognized stock-based compensation expense under the 2011 Stock Option and Incentive Plan, 2003 Stock Plan, 2011 Employee Stock Purchase Plan, the Incapsula 2010 Share Incentive Plan, and the SkyFence 2013 Share Incentive Plan (collectively the Plans) in the condensed consolidated statements of operations as follows (in thousands):

	For the three months ended June 30,		For the six months ended June 30,	
	2014	2013	2014	2013
Cost of revenues	$ 529	$ 255	$ 903	$ 468
Research and development	2,190	720	3,982	1,386
Sales and marketing	3,209	1,643	5,639	2,976
General and administrative	2,737	974	4,807	1,615
Total stock-based compensation expense	$ 8,665	$ 3,592	$ 15,331	$ 6,445

The fair value of stock option grants for the three months and six months ended June 30, 2014 and 2013 was estimated using the following weighted average assumptions:

	For the three months ended June 30,		For the six months ended June 30,	
	2014	**2013**	**2014**	**2013**
Stock option grants:				
Dividend rate	0%	0%	0%	0%
Risk-free interest rate	1.9%	1.1%	1.9%	1.1%
Expected term (in years)	6.1	6.0	6.1	6.0
Expected volatility	44%	48%	45%	46%
ESPP grants:				
Dividend rate	0%	0%	0%	0%
Risk-free interest rate	0.1%	0.1%	0.1%	0.1%
Expected term (in years)	0.5	0.5	0.5	0.5
Expected volatility	57%	48%	57%	48%

The fair value of the RSUs is determined using the closing price of the Company s common stock on the date of the grant. Compensation is recognized on a straight-line basis over the requisite service period of each grant adjusted for estimated forfeitures.

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The following table summarizes option activity under the Plans and related information:

	Options Outstanding			
	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Balances - January 1, 2014	1,675,506	$ 23.78	8.01	$ 40,813
Granted	779,005	47.45		
Exercised or released	(254,766)	10.75		
Cancelled or forfeited	(140,406)	32.14		
Options assumed in acquisitions	72,607	14.14		
Balances - June 30, 2014	2,131,946	$ 33.05	8.19	$ 9,541
Options exercisable	625,837	$ 19.72	6.65	$ 6,224

RSU Activity

A summary of RSU activity under the Plans for the six months ended June 30, 2014, is as follows:

	Number of Restricted Stock Units Outstanding	Weighted-Average Grant Date Fair Value
Unvested - January 1, 2014	1,044,651	$ 31.64
Granted	885,752	47.02
Granted, performance RSUs	16,000	58.02
Released	(144,611)	34.41
Cancelled or expired	(107,052)	38.98
RSUs assumed in acquisitions	204,828	61.40
Unvested - June 30, 2014	1,899,568	$ 41.62

The aggregate intrinsic value of options exercised under the Plans was $9.6 million for the six months ended June 30, 2014. The aggregate intrinsic value is calculated as the difference between the per-share exercise price and the market value of the Company s common stock for each share subject to an option multiplied by the number of shares subject to options. As reported in the Wall Street Journal, the market value as of June 30, 2014 was $26.18 per share. As of June 30, 2014, total compensation cost related to unvested stock-based awards granted to employees under the Plans, but not yet recognized, was $92.6 million, net of estimated forfeitures. As of June 30, 2014, this cost will be amortized to expense over a weighted-average remaining period of 3.1 years, and will be adjusted for subsequent changes in estimated forfeitures. Future stock-based award grants will increase the amount of compensation expense to be recorded in these periods.

There was no capitalized stock-based compensation cost tax benefits during the six months ended June 30, 2014 and 2013.

(f) Common Stock Subject to Repurchase

Pursuant to restricted stock agreements with the Company s CEO, the Company has the right, but not the obligation, to repurchase the unvested shares of common stock upon termination of employment at the original purchase price per share. The repurchase rights with respect to the common stock lapse over the vesting period, which ranges from 48 months to 60 months. The amounts received in exchange for these shares have been included in other liabilities in the accompanying condensed consolidated balance sheet and are reclassified to equity as the shares vest. The Company granted 843,819 shares of restricted common stock with a weighted-average grant date fair value per share of $1.94 during the year ended December 31, 2010. There were no grants of shares of restricted common stock during the six months ended June 30, 2014 and the years ended December 31, 2012 and 2011. As of June 30, 2014, 210,954 shares of restricted common stock held by the Company s CEO were unvested and subject to repurchase by the Company.

In connection with the acquisition of Skyfence in the first quarter of 2014, the Company agreed to exchange 532,262 shares with a fair value per share of $59.08 as part of the purchase consideration which are subject to forfeiture based upon time-based vesting and continuing employment over the term of the corresponding four-year service period. None of these shares were vested as of June 30, 2014.

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(g) Early Exercise of Stock Options

In 2010 and 2011, the Company s board of directors allowed for the early exercise of stock options granted to certain members of the Company s board of directors. The amounts received in exchange for these shares have been included in other liabilities in the accompanying condensed consolidated balance sheet and are reclassified to equity as the shares vest. As of June 30, 2014, 26,250 shares were unvested.

(h) Equity Awards Issued in Acquisitions

In connection with the SkyFence and Incapsula acquisitions, the Company assumed stock options covering an aggregate of 72,607 shares of its common stock (in addition to the Incapsula RSUs discussed above). At the date of the acquisition, vested stock options and the associated fair value was recorded as part of the purchase consideration. The fair value related to the assumed unvested stock options are recognized as post-combination compensation costs and is being recorded as post-combination compensation expense ratably over the respective remaining service periods.

11. Accumulated Other Comprehensive Income (Loss)

The changes in the balances of accumulated other comprehensive income (loss) by component are as follows (in thousands):

	For the three months ended June 30, 2014			For the three months ended June 30, 2013		
	Unrealized gain (loss) on cash flow hedges	Unrealized gain (loss) on investments	Total	Unrealized gain (loss) on cash flow hedges	Unrealized gain (loss) on investments	Total
Balance at April 1	$ (426)	$ 1	$ (425)	$ 827	$ 104	$ 931
Other comprehensive income (loss) before reclassifications	76	11	87	207	(62)	145
Amounts reclassified to net loss	5		5	(441)	(79)	(520)
Other comprehensive income (loss)	81	11	92	(234)	(141)	(375)
Balance at June 30	$ (345)	$ 12	$ (333)	$ 593	$ (37)	$ 556

	For the six months ended June 30, 2014			For the six months ended June 30, 2013		
	Unrealized gain (loss) on cash flow hedges	Unrealized gain (loss) on investments	Total	Unrealized gain (loss) on cash flow hedges	Unrealized gain (loss) on investments	Total
Balance at January 1	$ (426)	$ (2)	$ (428)	$ 690	$ 171	$ 861
Other comprehensive income (loss) before reclassifications	76	14	90	486	(46)	440
Amounts reclassified to net loss	5		5	(583)	(162)	(745)

Other comprehensive income (loss)	81	14	95	(97)	(208)	(305)
Balance at June 30	$ (345)	$ 12	$ (333)	$ 593	$ (37)	$ 556

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The following is a summary of reclassifications out of accumulated other comprehensive income (loss) for the six months ended June 30, 2014 and 2013 (in thousands):

	For the three months ended June 30, 2014			For the three months ended June 30, 2013		
	Pre-Tax Amount	Tax Expense (Benefit)	After-Tax Amount	Pre-Tax Amount	Tax Expense (Benefit)	After-Tax Amount
Unrealized gains (losses) on cash flow hedges:						
Current period unrealized gain (loss)	$ 118	$ (42)	$ 76	$ 59	$ 148	$ 207
Reclassification adjustments[1]	10	(5)	5	(360)	(81)	(441)
Unrealized gains (losses) on cash flow hedges, net	128	(47)	81	(301)	67	(234)
Unrealized gains (losses) on investments:						
Current period unrealized gain (loss)	21	(10)	11	(62)		(62)
Reclassification adjustments[2]				(79)		(79)
Unrealized gains (losses) on investments	21	(10)	11	(141)		(141)
Other comprehensive income/(loss)	$ 149	$ (57)	$ 92	$ (442)	$ 67	$ (375)

	For the six months ended June 30, 2014			For the six months ended June 30, 2013		
	Pre-Tax Amount	Tax Expense (Benefit)	After-Tax Amount	Pre-Tax Amount	Tax Expense (Benefit)	After-Tax Amount
Unrealized gains (losses) on cash flow hedges:						
Current period unrealized gain (loss)	$ 118	$ (42)	$ 76	$ 486	$	$ 486
Reclassification adjustments[1]	10	(5)	5	(583)		(583)
Unrealized gains (losses) on cash flow hedges, net	128	(47)	81	(97)		(97)
Unrealized gains (losses) on investments:						
Current period unrealized gain (loss)	26	(12)	14	(46)		(46)
Reclassification adjustments[2]				(162)		(162)

Unrealized gains (losses) on investments	26	(12)	14	(208)		(208)
Other comprehensive income/(loss)	$ 154	$ (59)	$ 95	$ (305)	$	$ (305)

[1] Refer to note 6 for the affected line items in the condensed consolidated statement of operations
[2] Amount included in other income (expense), net, in the condensed consolidated statement of operations

12. Income Taxes

The Company is subject to income tax in the United States as well as other tax jurisdictions in which it conducts business. Earnings from non-U.S. activities are subject to local country income tax. The Company does not provide for federal income taxes on the undistributed earnings of its foreign subsidiaries as such earnings are to be reinvested indefinitely. The Company recorded income tax expense (benefit) of $(35,000) and $0.3 million for the three months ended June 30, 2014 and 2013, respectively and $(0.4) million and $0.4 million for the six months ended June 30, 2014 and 2013, respectively. These income tax expense (benefit) amounts were primarily attributable to foreign taxes.

Factors that impact the income tax provision include, but are not limited to, stock-based compensation expense, permanent tax adjustments, foreign operations and a valuation allowance against the Company s deferred tax assets.

13. Segment Information

During the three months ended March 31, 2014, we revised our business segments based upon the acquisition of the remaining shares of Incapsula, Inc. that the Company did not already own. As a result, the Company no longer separately reports the Incapsula segment and the Company now operates its business in one operating segment, which is the development, marketing, sales, service and support of data center security solutions that protect high value applications and data assets in physical and virtual data centers. Operating segments are defined as components of an enterprise that engage in business activities for which separate financial information is available and evaluated by the chief operating decision maker in deciding how to allocate resources and assessing performance. The chief operating decision maker is the Company s Chief Executive Officer.

The Company s net services revenue is comprised of the following (in thousands):

	For the three months ended June 30,		For the six months ended June 30,	
	2014	2013	2014	2013
Maintenance and support	$ 13,522	$ 10,673	$ 26,185	$ 20,787
Professional services and training	3,081	2,496	5,380	4,771
Subscriptions	5,253	2,499	9,836	4,541
Total net services revenue	$ 21,856	$ 15,668	$ 41,401	$ 30,099

The Company s net revenue by geographic region, based on the customer s location, is summarized as follows (in thousands):

	For the three months ended June 30,		For the six months ended June 30,	
	2014	2013	2014	2013
Americas	$ 22,854	$ 20,048	$ 40,930	$ 38,227
EMEA	9,404	6,223	17,614	12,502
APAC	6,184	5,068	11,414	9,195
Total net revenue	$ 38,442	$ 31,339	$ 69,958	$ 59,924

The following table presents long-lived assets by location (in thousands):

	As of June 30, 2014	As of December 31, 2013
United States	$ 6,520	$ 3,039
Israel	10,286	2,422
Other	29	14
Total long-lived assets	$ 16,835	$ 5,475

14. Net Loss per Share

The following outstanding shares of common stock and potential common shares were excluded from the computation of diluted net loss per share of common stock for the periods presented because including them would have been antidilutive:

	For the three months and six months ended June 30,	
	2014	2013
Stock options to purchase common stock	2,131,946	2,031,257
Restricted stock units for common stock	1,899,568	873,207
Restricted shares of common stock subject to repurchase	237,204	432,920
Restricted stock issued in connection with Skyfence acquisition	354,678	

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the (1) unaudited condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q, and (2) the audited consolidated financial statements and notes thereto and management s discussion and analysis of financial condition and results of operations for the year ended December 31, 2013 included in our Annual Report on Form 10-K filed with the Securities and Exchange Commission, or the SEC, on February 28, 2014. This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements are often identified by the use of words such as may, will, expect, believe, anticipate, intend, could, estimate, or continue, and similar expressions or variations. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified herein, and those discussed in the section titled Risk Factors, set forth in Part II, Item 1A of this Form 10-Q and in our other SEC filings, including our Annual Report on Form 10-K for the year ended December 31, 2013. You should review these risk factors for a more complete understanding of the risks associated with an investment in our securities. We disclaim any obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We are pioneering the third pillar of enterprise security, data center security, by directly protecting high-value applications and data assets in physical and virtual data centers. Built specifically for modern threats, our comprehensive suite of data center security offerings is designed to provide the visibility and control needed to neutralize attacks, theft and fraud from inside and outside the organization, mitigate risk, and streamline compliance. Our SecureSphere platform provides database, file and web application security across various physical and virtual systems in data centers, including traditional on-premise data centers as well as private, public and hybrid cloud computing environments. In addition, our cloud offerings are designed to protect against the unique threats created as enterprises increasingly shift to deploying their applications and storing their data in the cloud to take advantage of the flexibility and cost-efficiency offered by cloud-based solutions.

We believe that data center security is the third pillar of enterprise security because it fills the gaps between the first pillar of security, endpoint security, which blocks threats targeting devices, and the second pillar of security, network security, which blocks threats trying to access the network. Our unique suite of offerings protects the high-value applications and data assets that endpoint and network solutions are not designed to protect, whether the applications and data reside within our customers data center or the cloud.

Organizations are facing numerous challenges in providing the visibility and control required to protect high-value applications and data assets from attack, theft and fraud. Attacks, whether perpetrated by sophisticated hackers or malicious insiders, continue to increase in sophistication, scale and frequency, and organizations must comply with increasingly complex regulatory standards enacted to protect high-value applications and data. Adoption of new technologies and architectures, such as mobile applications, modern web applications and big data, increases the complexity of, and open access to, the data center; thereby exposing critical data assets to new vulnerabilities. The increased adoption of cloud delivery models and virtualization technologies is also forcing applications to operate outside of the traditional security model. We believe that these challenges are driving the need for a comprehensive data center security solution to protect high-value applications and data assets in the data center.

We were incorporated as a Delaware corporation in 2002 with the vision of protecting high-value applications and data assets within the enterprise. Since that time we have been investing in our data center security solutions to meet the rapidly evolving demands of customers. We shipped our initial web application security and data security products in 2002; in 2006, we expanded our database security product to include compliance features. In 2010, we launched our file security offering. In addition, in 2010, we launched our cloud-based initiatives with ThreatRadar and, in 2011, we introduced our cloud-based offering for mid-market enterprises and small and medium-sized businesses (SMB) that we provide through Incapsula, Inc., which was majority owned by us until March 2014 when we acquired the remaining portion of Incapsula that we did not already own in order to more fully integrate their operations with ours. In January 2014, we acquired certain assets and liabilities of Tomium Software, LLC to accelerate our mainframe data security solutions. In February 2014, we acquired SkyFence Networks Ltd. to further our Software as a Service (SaaS) delivery models for internally facing corporate applications.

Our research and development efforts are focused primarily on improving and enhancing our existing data center security solutions and services, as well as developing new products and services and conducting advanced security research. We conduct our research and development activities in Israel, and we believe this provides us with access to some of the best engineering talent in the security industry. As of June 30, 2014, we had 248 employees dedicated to research and development, including our advanced security research group, the Application Defense Center (ADC). Our research and development expense was $21.6 million for the six months ended June 30, 2014 as compared to $13.0 million for the same period in 2013.

We derive our revenue from sales and licenses of our products and sales of our services. Products and license revenue is generated primarily from sales of perpetual software licenses installed on hardware appliances or virtual appliances for our SecureSphere Business Security Suite. Services revenue consists of maintenance and support, professional services and training and subscriptions. A majority of our revenue is derived from customers in the Americas region. In the six months ended June 30, 2014, 59% of our total revenue was generated from the Americas, 25% from Europe, Middle East and Africa (EMEA) and 16% from Asia Pacific (APAC).

We market and sell our products through a hybrid sales model, which combines a direct touch sales organization and an overlay channel sales team that actively assist our extensive network of channel partners throughout the sales process. We also provide our channel partners with marketing assistance, technical training and support. We primarily sell our products and services through our channel partners, including distributors and resellers, which sell to end-user customers, who we refer to in this Quarterly Report on Form 10-Q as our customers. We have a network of over 300 channel partners worldwide, including both resellers and distributors. In 2013, our channel partners originated over 40% and fulfilled almost 85% of our sales. We work with many of the world s leading security value-added resellers, and our partners include some of the largest hosting companies for cloud-based deployments.

As of June 30, 2014, we had over 3,300 customers in more than 90 countries, excluding direct customers of our Incapsula subsidiary. In addition, our solutions are used to protect thousands of organizations through cloud-based deployments with our SaaS customers and our managed security service provider (MSSP) and hosting partners. Our customers include top telecommunications companies, commercial banks in the United States, global consumer financial service firms, computer hardware companies, as well as over 250 government agencies around the world and more than 350 Global 2000 companies.

Our net revenue has increased in each of the last three years, growing from $78.3 million in 2011 to $137.8 million in 2013. We have incurred net losses attributable to our stockholders of $32.8 million in the six months ended June 30, 2014 and $25.2 million in the year ended December 31, 2013, respectively. As of June 30, 2014, we had an accumulated deficit of $131.5 million.

Opportunities, Challenges and Risks

We believe that the growth of our business and our future success are dependent upon many factors, including our ability to maintain our technology leadership, improve our sales and marketing, address the needs of smaller enterprises and compete effectively in the marketplace for data center security solutions. While each of these areas presents significant opportunities for us, they also pose important challenges and risks that we must successfully address in order to sustain the growth of our business and improve our results of operations.

Maintain Technology Leadership. As a result of the rise in sophisticated attacks by hackers and malicious insiders, the difficulty in complying with regulations governing business data and the growing complexity of, and open access to, data centers, we believe that enterprises are struggling to provide visibility and control over high-value business applications and data assets that they need to protect. In addition, organizations are increasingly taking advantage of cloud-based services and virtualization technologies, and these new technologies and architectures are increasing the complexity of, and accessibility to, the data center. We believe these challenges are driving the need for a new protection layer positioned closely around the applications and data assets in the data center. We expect that as enterprises recognize the growing risk to high-value business data and the need to comply with increasing regulatory compliance mandates, their spending will increase on solutions designed to control and protect such data. We believe that traditional security and compliance products do not address the evolving needs of enterprises or do not do so adequately, and that this presents us with a large market opportunity. To capitalize on this opportunity, we have introduced and expect that in the future we will need to continue to introduce innovations to our broad business

security solutions, including solutions to address data center security opportunities that arise as enterprises pursue cloud computing initiatives. We cannot assure you that our products will achieve widespread market acceptance or that we will properly anticipate future customer needs. Moreover, if our products do not satisfy evolving customer requirements, we will not capture the increase in spending that we expect will result from enterprises seeking to secure data across various systems in the data center.

Invest in Sales and Marketing. In order to capitalize on the anticipated increase in spending in the data center security market, we will need to continue to invest significant resources to further strengthen our existing relationships with channel partners, extend our global network by adding new channel partners and grow our sales and marketing team. Any investments that we make in our sales and marketing will occur in advance of our experiencing any benefits from such investments, and so it may be difficult for us to determine if we are efficiently allocating our resources in this area. We cannot assure you that the investments that we intend to make to strengthen our sales and marketing efforts will enable us to capitalize on the expected increase in spending in the data center security market or result in an increase in revenue or an improvement in our results of operations.

Address Needs of Smaller Enterprises. As market awareness of the benefits of a comprehensive data center security solution increases, we believe there is a significant opportunity to provide data center security solutions to smaller enterprises as they confront increasing security threats and compliance mandates. To capitalize on this opportunity, we intend to increase our business with mid-market enterprises and SMBs by expanding our cloud-based service offerings and our distribution channel. We have made, and may in the future continue to make, significant investments in our cloud-based security products to address the business security needs of mid-market enterprises and SMBs. If our cloud-based security products, which are relatively new, fail to gain broad acceptance with mid-market enterprises and SMBs, our revenue growth, results of operations and competitive position in our industry could suffer.

Compete Effectively. We operate in an intensely competitive market that has witnessed significant consolidation in recent years with large companies acquiring many of our competitors. We track our success rate in competitive sales opportunities against certain competitors, some of which generate higher revenues and have greater market capitalizations than we do, and many of which are more established or have greater name recognition within our industry. Based upon our internal tracking of the results of such competitive sales opportunities, we believe that we have historically competed favorably against our larger competitors, and that we have a proven track record of successfully competing against such larger competitors. Nonetheless, some of our larger competitors have numerous advantages, including, but not limited to, greater financial resources, broader product offerings and more established relationships with channel partners and customers. If we are unable to compete effectively for a share of the business security market, our business, results of operations and financial condition could be materially and adversely affected.

To date, we have incurred, and continue to incur, losses from operations and net losses. However, we believe that our existing cash, cash equivalents and short-term investments will be sufficient to meet our working capital and capital expenditure needs for at least the next 12 months. Further, we expect that, if we successfully execute our business plan and strategy, our loss from operations and our net losses will decline, and that we will reach profitability. Should we need additional cash in the future, we may utilize existing lines of credit, enter into additional lines of credit or raise funds through the sale of equity securities.

Key Metrics of Our Business

We monitor the key financial metrics discussed below to help us evaluate growth trends, establish budgets, measure the effectiveness of our sales and marketing efforts and assess operational efficiencies.

Net Revenue. We measure our net revenue to assess the acceptance of our products from our customers, our growth in the markets we serve and to help us establish our strategic and operating plans for future periods. We discuss the components of our net revenue in Financial Overview Net Revenue below.

Gross Margin. We monitor our gross margin to assess the impact on our current and forecasted financial results from any changes to the pricing and mix of products we are selling to our customers.

Loss from Operations. We track our loss from operations to assess how effectively we are planning and monitoring our operations as well as controlling our operational costs, which are primarily driven by headcount.

Cash, Cash Equivalents and Short-term Investments. We evaluate the level of our cash, cash equivalents and short-term investments to ensure we have sufficient liquidity to fund our operations, including the development of future products and product enhancements and the expansion into new sales channels and territories.

Number of Customers. We believe our customer count is a key indicator of our market penetration, the productivity of our sales organization and the value that our products bring to our customer base. We also believe our existing customers represent significant future revenue opportunities for us.

We discuss for the periods presented revenue, gross margin, the components of loss from operations and number of customers further below under Segments and Results of Operations , as applicable, and we discuss our cash and cash equivalents under Liquidity and Capital Resources.

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We also believe that deferred revenue and cash flow from operations are key financial metrics for our business. The components of deferred revenue and cash flow from operations, as well as our rationale for monitoring these metrics, are discussed immediately below this table:

	For the three months ended or As of June 30,		For the six months ended or As of June 30,	
	2014	2013	2014	2013
	(in thousands, except number of customers and percentages)			
Net revenue	$ 38,442	$ 31,339	$ 69,958	$ 59,924
Gross margin	76.5%	75.9%	76.0%	76.9%
Loss from operations	$ (15,258)	$ (5,729)	$ (33,099)	$ (11,723)
Total deferred revenue	$ 64,142	$ 48,303	$ 64,142	$ 48,303
Cash, cash equivalents and short-term investments	$ 99,479	$ 110,383	$ 99,479	$ 110,383
Net cash provided by (used in) operations	$ (6,809)	$ (796)	$ (3,633)	$ 6,897
Number of customers	3,357	2,626	3,357	2,626

Deferred Revenue

Our deferred revenue consists of amounts that have been invoiced but that have not yet been recognized as revenue. The majority of our deferred revenue balance consists of the unamortized portion of services revenue from maintenance and support contracts. We monitor our deferred revenue balance because it represents a significant portion of revenue to be recognized in future periods. We also assess the increase in our deferred revenue balance plus revenue we recognized in a particular period as a measure of our sales activity for that period. While the change in our deferred revenue and revenue recognized in a given period comprise the majority of our sales activity during that period, they do not constitute the entire sales activity during the period. Our total sales activity also includes sales of products and services for which we have not yet met the criteria to recognize revenue or add such amounts to our deferred revenue balance. Revenue and deferred revenue from these transactions is recognized or recorded in future periods when we have met the required criteria. We discuss for the periods presented deferred revenue further below under Results of Operations.

Net Cash Flow Provided By Operations

We monitor cash flow from operations as a measure of our overall business performance. Our cash flow from operations is driven primarily by sales of our products and licenses and, to a lesser extent, from up-front payments from customers under maintenance and support contracts. Our primary uses of cash in operating activities are for personnel-related expenditures, costs of acquiring the hardware used for our appliances, marketing and promotional expenses and costs related to our facilities. Monitoring cash flow from operations enables us to analyze our financial performance without the non-cash effects of certain items such as depreciation and amortization and stock-based compensation expenses, thereby allowing us to better understand and manage the cash needs of our business.

Segments

Effective January 1, 2014, we revised our business segments in order to better align them with our strategic approach to the markets and customers we serve. As a result, we no longer separately report the Incapsula segment and we now operate our business in one reportable segment, which is the development, marketing, sales, service and support of data center security solutions that protect high value applications and data assets in physical and virtual data centers.

Operating segments are defined as components of an enterprise that engage in business activities for which separate financial information is available and evaluated by the chief operating decision maker in deciding how to allocate resources and assessing performance. The chief operating decision maker is the Company s Chief Executive Officer.

Financial Overview

Net Revenue

We derive our revenue from sales and licenses of our products and sales of our services.

Our net revenue is comprised of the following:

Products and License Revenue Product and license revenue is generated from sales of perpetual software licenses installed on hardware appliances or virtual appliances for our SecureSphere Business Security Suite. Our SecureSphere Business Security Suite consists of database security, file security and web application security. We offer multiple hardware appliance versions that accompany our software, each with different throughput capacities. Perpetual software license revenue is generated from sales of our appliances, licenses for additional users and add-on software modules. We also generate a small amount of hardware revenue from sales of spares or replacement appliances, demonstration units, third-party OEM units and accessories.

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Services Revenue Services revenue consists of maintenance and support, professional services and training and subscriptions. Maintenance and support revenue is generated from support services that are bundled with appliances and add-on software modules. There are three levels of maintenance and support Standard, Enhanced and Premium and these are offered through agreements for one to five-year terms. Maintenance and support includes major and minor if-and-when available software updates; customer care, which includes our designated support engineer program; content updates from our advanced security research group, the ADC, and hardware replacement. Subscription revenue is generated from sales of our cloud-based services. Professional services revenue consists of fees we earn related to implementation and consulting services we provide our customers. Training services revenue consists of fees we earn related to training customers and partners on the use of our products. We expect that the services revenue from maintenance and support contracts will continue to grow along with the increase in the size of our installed base.

Most of our products and services are sold to customers in the Americas, primarily in the U.S., however, a significant portion of our revenue is generated from international sales. See Note 13 of Notes to Condensed Consolidated Financial Statements for a discussion of our financial information by geographic region. Our revenue by geographic region is as follows:

	For the three months ended June 30,		For the six months ended June 30,	
	2014	2013	2014	2013
Americas	$ 22,854	$ 20,048	$ 40,930	$ 38,227
EMEA	9,404	6,223	17,614	12,502
APAC	6,184	5,068	11,414	9,195
Total net revenue	$ 38,442	$ 31,339	$ 69,958	$ 59,924

Cost of Revenue

Our total cost of revenue is comprised of the following:

Cost of Products and License Revenue Cost of products and license revenue is comprised primarily of third-party hardware costs and royalty fees. Our cost of products and license revenue also includes personnel costs related to our operations team, shipping costs and write-offs for excess and obsolete inventory.

Cost of Services Revenue Cost of services revenue is primarily comprised of personnel costs of our technical support team, our professional consulting services and training teams and our Security Operations Center (SOC) team. Cost of services revenue also includes facilities costs, subscription fees and depreciation. We expect that our cost of services revenue will increase in absolute dollars as we increase our headcount.

Operating Expenses

Our operating expenses consist of research and development, sales and marketing and general and administrative expenses. Personnel costs are the most significant component of our operating expenses and consist of wages, benefits and bonuses and, with regard to the sales and marketing expense, sales commissions. Personnel costs also include stock-based compensation. We expect operating costs to continue to increase in absolute dollars given our recent

acquisitions and the related costs associated with the acquired personnel and business.

Research and Development

Our research and development is focused on maintaining and improving our existing products and on new product development. A majority of our research and development expenses are comprised of personnel costs and, to a lesser extent, facility costs, hardware prototype costs, laboratory expenses and depreciation. We expense research and development costs as incurred. We expect our research and development expenses to increase in absolute dollars as we continue to enhance our existing products and develop or acquire new products and services that address the emerging market for business security and regulatory compliance.

Sales and Marketing

Sales and marketing expense is the largest component of our operating expenses and consists primarily of personnel costs, including commissions and travel expenses. Sales and marketing expenses also include costs related to marketing and promotional activities, third-party referral fees and, to a lesser extent, facilities costs and depreciation. We expect our sales and marketing expenses to increase in absolute dollars as we expand our sales and marketing efforts worldwide.

General and Administrative

General and administrative expense consists primarily of personnel costs as well as professional fees, facilities costs and depreciation. General and administrative personnel costs include our executive, finance, purchasing, order entry, human resources, information technology and legal functions. Our professional fees consist primarily of accounting, external legal, information technology and other consulting costs.

Amortization of acquired intangible assets

Intangible assets acquired through acquisitions are amortized in operating expenses.

Other Income (Expense), net

Other income (expense), net is comprised of the following items:

- Interest Income Interest income consists of interest earned on our cash, cash equivalents and short-term investments. We expect interest income will vary each reporting period depending on our average investment balances during the period and market interest rates.

- Interest Expense Interest expense consists of interest accrued or paid on debt obligations.

- Foreign Currency Forward Contract Gains (Losses) Foreign currency forward contract gains and losses pertain to the ineffective portion of derivative instruments that we have entered into primarily to manage our exposure to the variability in expected future expenses resulting from changes in foreign currency exchange rates. We do not use derivative financial instruments for speculative or trading purposes. We expect our foreign currency forward contract gains (losses) to continue to fluctuate in the future due to changes in foreign currency exchange rates.

- Foreign Currency Exchange Gains (Losses) Foreign currency exchange gains and losses relate to transactions denominated in currencies other than the U.S. Dollar.

Provision for Income Taxes

We operate in several tax jurisdictions and are subject to taxes in each country or jurisdiction in which we conduct business including the United States and Israel. Earnings from our non-U.S. activities are subject to local country income tax and may be subject to U.S. income tax if such earnings are distributed to the U.S. To date, we have incurred net losses and have recorded insignificant U.S. federal income tax expense. Our tax expense to date relates to foreign income taxes, mainly from our Israeli and United Kingdom activities, and to a lesser extent, state income taxes.

Results of Operations

The following table is a summary of our consolidated statements of operations in dollars and as a percentage of our total revenue. We have derived the data for the three and six months ended June 30, 2014 and 2013 from our

condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q.

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	For the three months ended June 30,				For the six months ended June 30,			
	2014		2013		2014		2013	
	Amount	% of Net Revenue	Amount	% of Net Revenue	Amount	% of Net Revenue	Amount	% of Net Revenue
Net revenue:								
Products and license	$ 16,586	43.1%	$ 15,671	50.0%	$ 28,557	40.8%	$ 29,825	49.8%
Services:								
Maintenance and support	13,522	35.2%	10,673	34.0%	26,185	37.4%	20,787	34.7%
Professional services and training	3,081	8.0%	2,496	8.0%	5,380	7.7%	4,771	7.9%
Subscriptions	5,253	13.7%	2,499	8.0%	9,836	14.1%	4,541	7.6%
Total Services	21,856	56.9%	15,668	50.0%	41,401	59.2%	30,099	50.2%
Total net revenue	38,442	100.0%	31,339	100.0%	69,958	100.0%	59,924	100.0%
Cost of revenue:								
Products and license	2,075	5.4%	2,446	7.8%	3,807	5.4%	4,322	7.2%
Services	6,959	18.1%	5,098	16.3%	12,979	18.6%	9,513	15.9%
Total cost of revenue	9,034	23.5%	7,544	24.1%	16,786	24.0%	13,835	23.1%
Gross profit	29,408	76.5%	23,795	75.9%	53,172	76.0%	46,089	76.9%
Operating expenses:								
Research and development	11,618	30.2%	6,646	21.2%	21,579	30.8%	13,004	21.7%
Sales and marketing	25,065	65.2%	18,281	58.3%	48,100	68.8%	35,828	59.8%
General and administrative	7,621	19.8%	4,597	14.7%	16,026	22.9%	8,980	15.0%
Amortization of purchased intangibles	362	1.0%		0.0%	566	0.8%		0.0%
Total operating expenses	44,666	116.2%	29,524	94.2%	86,271	123.3%	57,812	96.5%
Loss from operations	(15,258)	-39.7%	(5,729)	-18.3%	(33,099)	-47.3%	(11,723)	-19.6%
Other income (expense), net	(215)	-0.6%	(55)	-0.2%	(369)	-0.5%	(102)	-0.2%
Loss before provision for income taxes	(15,473)	-40.3%	(5,784)	-18.5%	(33,468)	-47.8%	(11,825)	-19.8%
Provision for income taxes	(35)	-0.1%	261	0.8%	(406)	-0.5%	415	0.7%
Net loss	(15,438)	-40.2%	(6,045)	-19.3%	(33,062)	-47.3%	(12,240)	-20.5%
Loss attributable to noncontrolling interest		0.0%	130	0.4%	213	0.3%	266	0.5%

Net loss attributable to Imperva, Inc. stockholders	$ (15,438)	-40.2%	$ (5,915)	-18.9%	$ (32,849)	-47.0%	$ (11,974)	-20.0%

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Comparison of the Three Months and Six Months Ended June 30, 2014 and 2013

	For the three months ended June 30,		Change		For the six months ended June 30,		Change	
	2014	2013	Amount	%	2014	2013		
	(dollars in thousands)							
Net revenue:								
Products and license	$ 16,586	$ 15,671	$ 915	5.8%	$ 28,557	$ 29,825	$ (1,268)	-4.3%
Percentage of net revenue	43.1%	50.0%			40.8%	49.8%		
Services:								
Maintenance and support	13,522	10,673	2,849	26.7%	26,185	20,787	5,398	26.0%
Percentage of net revenue	35.2%	34.0%			37.4%	34.7%		
Professional services and training	3,081	2,496	585	23.4%	5,380	4,771	609	12.8%
Percentage of net revenue	8.0%	8.0%			7.7%	7.9%		
Subscriptions	5,253	2,499	2,754	110.2%	9,836	4,541	5,295	116.6%
Percentage of net revenue	13.7%	8.0%			14.1%	7.6%		
Total Services	21,856	15,668	6,188	39.5%	41,401	30,099	11,302	37.5%
Percentage of net revenue	56.9%	50.0%			59.2%	50.2%		
Total net revenue	$ 38,442	$ 31,339	$ 7,103	22.7%	$ 69,958	$ 59,924	$ 10,034	16.7%
Americas	$ 22,854	$ 20,048	$ 2,806	14.0%	$ 40,930	$ 38,227	$ 2,703	7.1%
Percentage of net revenue	59.5%	64.0%			58.5%	63.8%		
EMEA	9,404	6,223	3,181	51.1%	17,614	12,502	5,112	40.9%
Percentage of net revenue	24.5%	19.8%			25.2%	20.9%		
APAC	6,184	5,068	1,116	22.0%	11,414	9,195	2,219	24.1%
Percentage of net revenue	16.1%	16.2%			16.3%	15.3%		
Total net revenue	$ 38,442	$ 31,339	$ 7,103	22.7%	$ 69,958	$ 59,924	$ 10,034	16.7%

Three Months Ended June 30, 2014 Compared with Three Months Ended June 30, 2013

Our net revenue increased by $7.1 million, or 22.7%, to $38.4 million during the three months ended June 30, 2014 from $31.3 million during the three months ended June 30, 2013 primarily due to growth in services revenue. This revenue growth reflects the increasing demand for our subscription service offerings as well as a broader installed

base of product and licenses which generate higher maintenance and support revenues. The EMEA region contributed the largest portion of this growth with a $3.2 million increase over the same period in 2013 while revenue for the Americas region grew by $2.8 million. The revenue growth in the EMEA region in the three months ended June 30, 2014 as compared to the three months ended June 30, 2013 was primarily due to increased services revenue as we increased our customer base and continued to renew expiring customer maintenance agreements, and increased revenue from subscription sales of our cloud-based services. The Americas region experienced a similar increase in services revenue.

Products and license revenue increased by $0.9 million, or 5.8%, to $16.6 million during the three months ended June 30, 2014 from $15.7 million during the three months ended June 30, 2013. The change in product and license revenue was mostly driven by an increase in the EMEA region in the three months ended June 30, 2014 compared to the three months ended June 30, 2013. This increase was due to increased sales volume of our products.

Services revenue increased by $6.2 million, or 39.5%, to $21.9 million during the three months ended June 30, 2014 from $15.7 million during the three months ended June 30, 2013. During the three months ended June 30, 2014, our services revenue was comprised of $13.5 million in maintenance and support, $3.1 million in professional services and training and $5.3 million in subscriptions. The change in services revenue in the three months ended June 30, 2014 from the three months ended June 30, 2013 was primarily due to an increase of $2.8 million in maintenance and support revenue resulting from our larger installed base, $0.6 million in professional services and training revenues, and $2.8 million in subscriptions revenue from our cloud-based security services and ThreatRadar.

Six Months Ended June 30, 2014 Compared with Six Months Ended June 30, 2013

Our net revenue increased by $10.0 million, or 16.7%, to $70.0 million during the six months ended June 30, 2014 from $59.9 million during the six months ended June 30, 2013 primarily due to growth in services revenue. This revenue growth reflects the increasing demand for our subscription service offerings as well as a broader installed base of product and licenses which generate higher maintenance and support revenues. The EMEA region contributed the largest portion of this growth with a $5.1 million increase over the same period in 2013. Revenue growth in the EMEA region in the six months ended June 30, 2014 as compared to the six months ended June 30, 2013 was primarily due to increased services revenue as we increased our customer base and continued to renew expiring customer maintenance agreements, increased revenue from subscription sales of our cloud-based services, and, to a lesser extent, increased sales of both product and licenses.

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Services revenue increased by $11.3 million, or 37.5%, to $41.4 million during the six months ended June 30, 2014 from $30.1 million during the six months ended June 30, 2013. During the six months ended June 30, 2014, our services revenue was comprised of $26.2 million in maintenance and support, $5.4 million in professional services and training and $9.8 million in subscriptions. The change in services revenue in the six months ended June 30, 2014 from the six months ended June 30, 2013 was primarily due to an increase of $5.4 million in maintenance and support revenue resulting from our larger installed base, $1.9 million in professional services and training revenues, and $5.3 million in subscriptions revenue from our cloud-based security services and ThreatRadar product.

Products and license revenue declined by $1.2 million, or 4.3%, to $28.6 million during the six months ended June 30, 2014 from $29.8 million during the six months ended June 30, 2013. The change in product and license revenue was mostly driven by a decrease of $3.1 million in the Americas region during the six months ended June 30, 2014 compared to the six months ended June 30, 2013. The decrease in the Americas region product and license revenue was primarily due to extended sales cycles for orders resulting from a combination of sales execution challenges in the United States and intensifying competition for orders exceeding $100,000.

Gross Profit

	For the three months ended June 30,			**For the six months ended June 30,**		
	2014	**2013**	**% Change**	**2014**	**2013**	**% Change**
			(dollars in thousands)			
Products and license	$ 14,511	$ 13,225		$ 24,750	$ 25,503	
Gross Margin %	87.5%	84.4%	3.1%	86.7%	85.5%	1.2%
Services gross profit	14,897	10,570		28,422	20,586	
Gross Margin %	68.2%	67.5%	0.7%	68.7%	68.4%	0.3%
Total gross profit	$ 29,408	$ 23,795		$ 53,172	$ 46,089	
Gross Margin %	76.5%	75.9%	0.6%	76.0%	76.9%	-0.9%

Three Months Ended June 30, 2014 Compared with Three Months Ended June 30, 2013

Total gross margin increased 0.6 percentage points from 75.9% during the three months ended June 30, 2013 to 76.5% during the three months ended June 30, 2014 primarily due to a products and license gross margin increase of 3.1% to 87.5% for the three months ended June 30, 2014 as compared to 84.4% for the three months ended June 30, 2013. The product and licenses gross margin improvement was primarily attributable to lower third-party product costs in the three months ended June 30, 2014 as compared to the comparable 2013 period as well as an increase in the proportion of virtual appliance to total appliance sales in the quarter ended June 30, 2014 as compared to the 2013 period. Virtual appliance sales tend to have higher gross margin percentages than physical appliances.

Six Months Ended June 30, 2014 Compared with Six Months Ended June 30, 2013

Total gross margin decreased 0.9 percentage points from 76.9% during the six months ended June 30, 2013 to 76.0% during the six months ended June 30, 2014 primarily due to an increased proportion of services revenue to total revenues for the six months ended June 30, 2014 as compared to the six months ended June 30, 2013.

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Operating Expenses

	For the three months ended June 30,		Change		For the six months ended June 30,		Change	
	2014	2013	Amount	%	2014	2013	Amount	%
	(dollars in thousands)							
Operating expenses:								
Research and development	$ 11,618	$ 6,646	$ 4,972	74.8%	$ 21,579	$ 13,004	8,575	65.9%
Percentage of net revenue	30.2%	21.2%			30.8%	21.7%		
Sales and marketing	25,065	18,281	6,784	37.1%	48,100	35,828	12,272	34.3%
Percentage of net revenue	65.2%	58.3%			68.8%	59.8%		
General and administrative	7,621	4,597	3,024	65.8%	16,026	8,980	7,046	78.5%
Percentage of net revenue	19.8%	14.7%			22.9%	15.0%		
Amortization of purchased intangibles	362		362	100.0%	566		566	100.0%
Percentage of net revenue	1.0%	0.0%			0.8%	0.0%		
Total operating expenses	$ 44,666	$ 29,524	$ 15,142	51.3%	$ 86,271	$ 57,812	$ 28,459	49.2%

Results above include stock-based compensation expense of:

	For the three months ended June 30,			For the six months ended June 30,		
	2014	2013	Change	2014	2013	Change
	(dollars in thousands)					
Cost of revenues	$ 529	$ 255	$ 274	$ 903	$ 468	$ 435
Research and development	2,190	720	1,470	3,982	1,386	2,596
Sales and marketing	3,209	1,643	1,566	5,639	2,976	2,663
General and administrative	2,737	974	1,763	4,807	1,615	3,192
	$ 8,665	$ 3,592	$ 5,073	$ 15,331	$ 6,445	$ 8,886

Three Months Ended June 30, 2014 Compared with Three Months Ended June 30, 2013

Research and development expenses increased by $5.0 million, or 74.8%, to $11.6 million during the three months ended June 30, 2014 from $6.6 million during the three months ended June 30, 2013. The change was primarily attributable to an increase of $4.3 million in personnel costs, including stock-based compensation, due to additional

research and development personnel being hired to support our ongoing product development efforts and Skyfence related research and development costs. In addition, we incurred increased third-party licensing costs of $0.4 million during the three months ended June 30, 2014.

Sales and marketing expenses increased by $6.8 million, or 37.1%, to $25.1 million during the three months ended June 30, 2014 from $18.3 million during the three months ended June 30, 2013. The change was principally related to an increase of $5.5 million in personnel costs, including stock-based compensation and contractor costs, due to increased headcount in all regions in an effort to help drive our overall revenue growth in addition to hiring related to our Skyfence acquisition. We also incurred increases in trade show, corporate marketing and seminar costs totaling $0.6 million.

General and administrative expenses increased by $3.0 million, or 65.8%, to $7.6 million during the three months ended June 30, 2014 from $4.6 million during the three months ended June 30, 2013. The change was primarily due to an increase of $2.5 million in personnel costs, including stock-based compensation, to build out our corporate level functions to support global growth in addition to headcount costs related to the acquisition of Skyfence.

Amortization of purchased intangibles increased by $0.4 million during the three months ended June 30, 2014 related to the acquisitions of Skyfence and Tomium completed during the first quarter of 2014. There was no such amortization in the prior year.

Six Months Ended June 30, 2014 Compared with Six Months Ended June 30, 2013

Research and development expenses increased by $8.6 million, or 65.9%, to $21.6 million during the six months ended June 30, 2014 from $13.0 million during the six months ended June 30, 2013. The change was primarily attributable to an increase of $7.7 million in personnel costs, including stock-based compensation, due to additional research and development personnel being hired to support our ongoing product development efforts and Skyfence related research and development costs. In addition, we incurred increased third-party licensing costs of $0.4 million during the three months ended June 30, 2014.

Sales and marketing expenses increased by $12.3 million, or 34.3%, to $48.1 million during the six months ended June 30, 2014 from $35.8 million during the six months ended June 30, 2013. The change was principally related to an increase of $9.3 million in personnel costs, including stock-based compensation and contractor costs, due to increased headcount in all regions in an effort to help drive our overall revenue growth in addition to hiring related to our Skyfence acquisition. Increases in trade show, corporate marketing and seminar costs, travel, and costs totaling $2.8 million also contributed to the increase in the six months ended June 30, 2014 as compared to the prior year comparable period.

General and administrative expenses increased by $7.0 million, or 78.5%, to $16.0 million during the six months ended June 30, 2014 from $9.0 million during the six months ended June 30, 2013. The change was primarily due to an increase of $4.9 million in personnel costs, including stock-based compensation, to build out our corporate level functions to support global growth in addition to headcount cost related to the acquisition of Skyfence. In addition, general and administrative expenses increased due to $1.4 million of legal and accounting costs related to the acquisitions of Skyfence, Tomium and the remaining interest in Incapsula that we did not previously own, all completed during the first quarter of 2014.

Amortization of purchased intangibles increased by $0.6 million during the six months ended June 30, 2014 related to the acquisitions of Skyfence and Tomium completed during the first quarter of 2014. There was no such amortization in the prior year.

Loss from Operations

Three months ended June 30,				Six months ended June 30,			
2014	2013	Change	% Change	2014	2013	Change	% Change
(dollars in thousands)							
$ (15,258)	$ (5,729)	$ (9,529)	-166.3%	$ (33,099)	$ (11,723)	$ (21,376)	-182.3%

Three Months Ended June 30, 2014 Compared with Three Months Ended June 30, 2013

Our loss from operations increased by $9.5 million, or 166.3%, to $15.3 million for the three months ended June 30, 2014 from $5.7 million for the three months ended June 30, 2013. Total operating expenses increased by $15.1 million during the three months ended June 30, 2014 when compared to the prior year period principally due to increases in personnel costs, including stock-based compensation expense, to support the increase in scope and global reach of our business and to incorporate the acquisitions of Skyfence and Tomium, which were closed in the first quarter of 2014. The increase in operating expenses was comprised of increased sales and marketing costs of $6.8 million to expand our global sales efforts, and an increase of $5.0 million of research and development costs to support our ongoing product development efforts and also new personnel associated with the Skyfence and Tomium acquisitions. In addition, we had increased general and administrative costs and amortization of purchased intangibles of $3.4 million, the majority of which was personnel expenses related to the acquired businesses. This increase in operating expenses was partially offset by an increase in our gross profit of $5.6 million during the three months ended June 30, 2014 due to higher net revenues.

Six Months Ended June 30, 2014 Compared with Six Months Ended June 30, 2013

Our loss from operations increased by $21.4 million, or 182.3%, to $33.1 million for the six months ended June 30, 2014 from $11.7 million for the six months ended June 30, 2013. Total operating expenses increased by $28.5 million during the six months ended June 30, 2014 when compared to the prior year period principally due to increases in personnel costs, including stock-based compensation expense, to support the increase in scope and global reach of our business and to incorporate the recently completed acquisitions of Skyfence and Tomium. The increase in operating expenses was comprised of increased sales and marketing costs of $12.3 million to expand our global sales efforts, and an increase of $8.6 million of research and development costs to support our ongoing product development efforts and also new personnel associated with the Skyfence and Tomium acquisitions. In addition, we had increased general and administrative costs and amortization of purchased intangibles totaling $7.6 million, the majority of which were personnel and legal expenses associated with the acquisition completed during the first quarter of 2014. This increase

in operating expenses was partially offset by an increase in our gross profit of $7.1 million during the six months ended June 30, 2014 due to higher net revenues.

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Other Income (Expense), net

Three months ended June 30,		Change		Six months ended June 30,		Change	
2014	**2013**	**Amount**	**%**	**2014**	**2013**	**Amount**	**%**
			(dollars in thousands)				
$ (215)	$ (55)	$ (160)	290.9%	$ (369)	$ (102)	$ (267)	-261.8%

Other income (expense) decreased by $0.2 million during the three months ended June 30, 2014 when compared to the three months ended June 30, 2013. The change was primarily due to a decrease of $0.1 million in foreign exchange losses, net, and a decrease of $0.1 million in investment income due to lower yields earned on invested balances.

Other income (expense) decreased by $0.3 million during the six months ended June 30, 2014 when compared to the six months ended June 30, 2013. The change was primarily due to a decrease of $0.1 million in foreign exchange losses, net, and a decrease of $0.2 million in investment income, net, due to lower yields earned on invested balances and interest expense accrued for a cash holdback liability in connection with the Skyfence acquisition.

Provision (Benefit) for Income Taxes

	2014	2013	Amount	%	2014	2013	Amount	%
					(dollars in thousands			
Provision (benefit) for income taxes	$ (35)	$ 261	$ (296)	-113.4%	$ (406)	$ 415	$ (821)	-197.8%
Effective tax rate	0.2%	-4.5%			1.2%	-3.5%		

The provision (benefit) for income taxes for the three months ended June 30, 2014 and 2013 is comprised primarily of foreign income taxes. During the three months ended June 30, 2014, the benefit is primarily attributable to the recognition of deferred tax assets for foreign losses incurred totaling $0.3 million.

The provision for income taxes for the six months ended June 30, 2014 and 2013 is comprised primarily of foreign income taxes. During the six months ended June 30, 2014, the benefit is primarily attributable to the recognition of deferred tax assets for foreign losses incurred totaling $0.9 million.

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Deferred Revenue

	As of June 30,		Change	
	2014	2013	Amount	%
	(dollars in thousands)			
Total deferred revenue	$ 64,142	$ 48,303	$ 15,839	32.8%

Deferred revenue increased by $15.8 million, or 32.8%, to $64.1 million as of June 30, 2014 from $48.3 million as of June 30, 2013. The growth in our deferred revenue was primarily attributable to an increase in our installed base of products and licenses worldwide and resulting renewals of maintenance and support agreements, as well as new sales of maintenance and support, and subscription agreements.

Number of Customers

	As of June 30,		Change	
	2014	2013	Amount	%
	(dollars in thousands)			
Number of customers	3,357	2,626	731	27.8%

Our number of customers increased by 731, or 27.8%, to 3,357 as of June 30, 2014 from 2,626 as of June 30, 2013. Our growth in customer count was driven by increasing market acceptance of our products as well as an increase in our global sales and services and support organizations from 265 people as of June 30, 2013 to 316 as of June 30, 2014. The growth in our sales and services and support organizations was consistent with our plans to continue expanding our global sales and support coverage, in particular for our channel partner sales and support teams. The increase in our services and support organization allowed us to target new customers while continuing to support our existing customers across all of our geographies.

Liquidity and Capital Resources

To date, we have satisfied our capital and liquidity needs through sales of our products and services, our initial public offering of common stock, and private placements of convertible preferred stock. We have incurred significant losses as we continue to expand our business. Our cash flow from operating activities will continue to be affected principally by the extent to which our revenue exceeds or does not exceed any increase in spending on personnel to support the growth of our business. Our largest source of operating cash flow is cash collections from our customers.

Capital Resources

As of June 30, 2014, we had $99.5 million of cash, cash equivalents and short-term investments, $3.7 million of which is currently held outside of the United States and not presently available to fund domestic operations and obligations. If we were to repatriate cash held outside of the United States, it could be subject to U.S. income taxes on such amounts, less any previously paid foreign income taxes. Our cash, cash equivalents and short-term investments have increased from $17.7 million as of December 31, 2010 to $99.5 million as of June 30, 2014. This increase is primarily the result of our initial public offering of common stock in November 2011 in which we raised $86.2 million, after deducting underwriters discounts and offering expenses. We believe our existing cash, cash equivalents and short-term investments will be sufficient to meet our working capital and capital expenditure needs for at least the next 12 months. Our future capital requirements may vary materially from those currently planned and will depend on

many factors, including, among other things, market acceptance of our products, the cost of our research and development activities, the acquisition of other businesses and overall economic conditions.

As of June 30, 2014, we had no amounts outstanding under our credit facility agreement with a financial institution. The credit facility agreement, as amended, provides for borrowing capacity up to $6.0 million and contains a minimum cash and cash equivalents balance covenant of $3.0 million. The credit facility expires on May 1, 2015. As of June 30, 2014, we were compliant with the covenant of the credit facility.

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Cash Flows

The following summary of our cash flows for the periods indicated has been derived from our consolidated financial statements which are included elsewhere in this Quarterly Report on Form 10-Q:

	Six months ended June 30	
	2014	2013
	(dollars in thousands)	
Net cash provided by (used in) operating activities	$ (3,633)	$ 6,897
Net cash provided by (used in) investing activities	(13,304)	1,192
Net cash provided by financing activities	3,223	2,893

Cash Flows from Operating Activities

Our largest uses of cash from operating activities are for employee related expenditures. Our primary source of cash flow from operating activities is cash receipts from customers. Our cash flow from operations will continue to be affected principally by the extent to which we grow our revenues and increase our headcount, primarily in our sales and marketing and research and development functions, in order to grow our business.

Net cash used in operating activities of $3.6 million for the six months ended June 30, 2013 reflected a net loss of $33.1 million, adjusted for non-cash charges of $17.8 million, as well as a net change of $11.6 million in our net operating assets and liabilities. The net change in our operating assets and liabilities was primarily the result of a decrease in our accounts receivable of $10.8 million.

Net cash provided by operating activities of $6.9 million for the six months ended June 30, 2013 reflected a net loss of $12.2 million, adjusted for non-cash charges of $8.1 million, as well as a net change of $11.0 million in our net operating assets and liabilities. The net change in our operating assets and liabilities was primarily the result of a decrease in our accounts receivable of $8.5 million, an increase in accrued compensation and benefits of $1.4 million and an increase in deferred revenue of $2.0 million, which represents unearned amounts billed to our customers, resulting from our larger installed base combined with strong maintenance and support renewal rates from our existing customers.

Cash Flows from Investing Activities

Our investing activities consist primarily of cost of acquisitions, expenditures to purchase property and equipment and purchases and sales of short-term investments. Cash used in investing activities during the six months ended June 30, 2014 was $13.3 million, primarily resulting from the acquisitions of Skyfence and Tomium for $12.1 million in addition to $2.8 million in capital expenditures, partially offset by net proceeds from the maturity of short-term investments of $2.0 million.

During the six months ended June 30, 2013, cash provided by investing activities was $1.2 million, primarily as a result of $29.4 million in maturities of short-term investments partially offset by $1.2 million in capital expenditures and $27.0 in purchases of short-term investments.

Cash Flows from Financing Activities

Net cash provided by financing activities was $3.2 million for the six months ended June 30, 2014 primarily as a result of proceeds received from the exercise of stock options and sale of common stock under our employee stock purchase plan.

Net cash provided by financing activities was $2.9 million for the six months ended June 30, 2013 primarily as a result of proceeds received from the exercise of stock options and sale of common stock under our employee stock purchase plan.

Contractual Obligations

The following summarizes our contractual obligations as of June 30, 2014:

	Payments Due by Period						
Contractual Obligations:	**2014**	**2015**	**2016**	**2017**	**2018**	**Thereafter**	**Total**
Operating lease obligations(1)	$ 2,922	$ 5,761	$ 5,731	$ 4,973	$ 3,443	$ 347	$ 23,177
Severance Pay Fund(2)							5,078
Purchase commitments(3)							5,877
Total	$ 2,922	$ 5,761	$ 5,731	$ 4,973	$ 3,443	$ 347	$ 34,132

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(1) Operating lease agreements represent our obligations to make payments under our non-cancelable lease agreements for our facilities. During the six months ended June 30, 2014, we made regular lease payments of $2.0 million under the operating lease agreements.
(2) Our consolidated balance sheet as of June 30, 2014 includes $5.1 million of non-current liabilities for our Israeli severance pay fund. The specific timing of any cash payments relating to this obligation cannot be projected with reasonable certainty and, therefore, no amounts for this obligation are included in the annual columns of the table set forth above.
(3) Purchase commitments are contractual obligations to purchase hardware appliances and related component parts from our vendors in advance of anticipated sales.

Off-Balance Sheet Arrangements

Through June 30, 2014, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations is based upon our Condensed Consolidated Financial Statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates, assumptions and judgments that can have significant impact on the reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. We base our estimates, assumptions and judgments on historical experience and various other factors that we believe to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. On a regular basis we evaluate our estimates, assumptions and judgments and make changes accordingly.

We believe that the estimates, assumptions and judgments involved in revenue recognition, stock-based compensation, long-lived assets, and accounting for income taxes have the greatest potential impact on our Consolidated Financial Statements, so we consider these to be our critical accounting policies. Historically, our estimates, assumptions and judgments relative to our critical accounting policies have not differed materially from actual results. The critical accounting estimates associated with these policies are described in Part II, Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations of our 2013 Annual Report on Form 10-K for the fiscal year ended December 31, 2013. Other than the change to our segment reporting and our policy for goodwill and acquired intangible assets, as more fully described in Note 1 to our Condensed Consolidated Financial Statements, there have been no material changes to our significant accounting policies as compared to the significant accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2013.

Recent Accounting Pronouncements

See Note 1 to the unaudited condensed consolidated financial statements in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no significant changes in our market risk exposures during the six months ended June 30, 2014 as compared to the market risk exposures disclosed in Management s Discussion and Analysis of Financial Condition and Results of Operations, set forth in Part II, Item 7A, of our Annual Report on Form 10-K for the year ended December 31, 2013.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation and supervision of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 under the Securities Exchange Act of 1934, or the Exchange Act. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based on the aforementioned evaluation, our chief executive officer and chief financial officer have concluded that as of June 30, 2014, our disclosure controls and procedures are designed at a reasonable assurance level and are effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure and that such controls and procedures provide reasonable assurance that the financial reporting and the preparation of financial statements for external purposes are reliably prepared and reported in accordance with generally accepted accounting principles.

Changes in Internal Control over Financial Reporting

Regulations under the Exchange Act require public companies, including our company, to evaluate any change in our internal control over financial reporting as such term is defined in Rule 13a-15(f) and Rule 15d-15(f) of the Exchange Act. In connection with their evaluation of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q, our chief executive officer and chief financial officer did not identify any changes in our internal control over financial reporting during the six months covered by this Quarterly Report that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we may be subject to legal proceedings and claims in the ordinary course of business.

On April 11, 2014, a purported shareholder class action lawsuit was filed in the United States District Court for the Northern District of California against Imperva and certain of its officers. The lawsuit purports to bring suit on behalf of those investors who purchased Imperva s publicly traded securities between May 2, 2013 and April 9, 2014. The plaintiff alleges that defendants made false and misleading statements, purports to assert claims for violations of the federal securities laws, and seeks unspecified compensatory damages and other relief. A response to the complaint is not yet due.

On June 27, 2014, a purported shareholder derivative lawsuit was filed in the Court of Chancery for the State of Delaware against Imperva (as a nominal defendant), and naming certain officers and members of Imperva s board of directors as individual defendants. The lawsuit relates to the acquisition of Skyfence Networks, Ltd. and the complaint asserts claims for breach of fiduciary duty and unjust enrichment, and seeks to recover unspecified compensatory damages allegedly sustained by Imperva, corporate reforms, the recovery of plaintiffs attorney s fees and other relief. A response to the complaint is not yet due.

In addition, we have received, and may in the future continue to receive, claims from third parties asserting, among other things, infringement of their intellectual property rights. Future litigation may be necessary to defend ourselves, our channel partners and our customers by determining the scope, enforceability and validity of third-party proprietary rights or to establish our proprietary rights.

Further, the ultimate outcome of any litigation is uncertain and, regardless of outcome, litigation can have an adverse impact on us because of defense costs, potential negative publicity, diversion of management resources and other factors. Accordingly, there can be no assurance that existing or future legal proceedings arising in the ordinary course of business or otherwise will not have a material adverse effect on our business, consolidated financial position, results of operations or cash flows.

Item 1A. Risk Factors

Risks Related to Our Business

We have a history of losses, we may not become profitable and our revenue growth may not continue.

We have incurred net losses in each fiscal year since our inception, including net losses attributable to our stockholders of $10.3 million in 2011, $7.4 million in 2012, $25.2 million in 2013 and $32.8 million in the six months

ended June 30, 2014. As a result, we had an accumulated deficit of $131.5 million at June 30, 2014. We may not become profitable in the future if we fail to increase revenue and manage our expenses, or if we incur unanticipated liabilities. Revenue growth may slow or revenue may decline for a number of possible reasons, including slowing demand for our products or services, increasing competition, a decrease in the growth of, or decline in, our overall market, or our failure to capitalize on growth opportunities or introduce new products and services. In addition, we have incurred, and anticipate that we will continue to incur, significant legal, accounting and other expenses relating to being a public company. If our revenues do not increase at a rate to proportionally offset these expected increases in operating expenses, our operating margins will suffer. Further, in future periods, our revenues could decline and, accordingly, we may not be able to achieve profitability and our losses may increase. Even if we do achieve profitability, we may not be able to sustain or increase profitability on a consistent basis. Any failure by us to achieve, maintain or increase profitability and continue our revenue growth could cause the price of our common stock to materially decline.

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Our quarterly operating results are likely to vary significantly and to be unpredictable, which could cause the trading price of our stock to decline.

Our revenues and operating results could vary significantly from period to period as a result of a variety of factors, many of which are outside of our control. As a result, comparing our revenues and operating results on a period-to-period basis may not be meaningful, and you should not rely on our past results as an indication of our future performance. We may not be able to accurately predict our future revenues or results of operations. We base our current and future expense levels on our operating plans and sales forecasts, and our operating costs are relatively fixed in the short-term. As a result, we may not be able to reduce our costs sufficiently to compensate for an unexpected shortfall in revenues, and even a small shortfall in revenues could disproportionately and adversely affect financial results for that quarter. In addition, we recognize revenues from sales to some customers or resellers when cash is received, which may be delayed because of issues with those customers or resellers. If our revenues or operating results fall below the expectations of investors or any securities analysts that cover our stock, the price of our common stock could decline substantially.

In addition to other risk factors listed in this section, factors that may individually or cumulatively affect our operating results from period to period include:

- the level of demand for our products and services, and the timing of orders from our channel partners and end-user customers, whom we refer to in this Quarterly Report on Form 10-Q as our customers;

- the timing of sales and shipments of products during a quarter, which may depend on many factors such as inventory and logistics and our ability to ship new products on schedule and accurately forecast inventory requirements;

- the mix of products sold, the mix of revenue between products and services, including subscription services, and the degree to which products and services are bundled and sold together for a package price;

- the budgeting, procurement and work cycles of our customers, which may result in seasonal variation as our business and the market for solutions such as ours mature;

- changes in customer renewal rates for our services;

- general economic conditions, both domestically and in our foreign markets, and economic conditions specifically affecting industries in which our customers participate;

- the timing of satisfying revenue recognition criteria for our sales, particularly where we accrue the associated commission expense in a different period, which may be affected by the mix of sales by our channel partners, the extent to which we bring on new resellers and distributors and establishing vendor-specific objective evidence of fair value, or VSOE, for new products and maintaining VSOE for maintenance and

services;

future accounting pronouncements or changes in our accounting policies; and

increases or decreases in our expenses caused by fluctuations in foreign currency exchange rates, since a significant portion of our expenses are incurred and paid in the Israeli shekel and other currencies besides the U.S. dollar.

Reliance on a concentration of shipments at the end of the quarter could cause our revenue to fall below expected levels, resulting in a decline in our stock price.

Historically, we have received a significant majority of a quarter s sales orders and generated a significant majority of a quarter s revenue during the last two weeks of the quarter. The fact that so many orders arrive at the end of a quarter means that our revenue may move from one quarter to the next if we cannot fulfill all of the orders and satisfy all of the revenue recognition criteria under our accounting policies before the quarter ends.

This pattern is a result of customer buying habits and the efforts of our sales force and channel partners to meet or exceed quarterly quotas. If expected revenue at the end of any quarter is delayed because anticipated purchase orders fail to materialize, our logistics partners fail to ship products on time, we fail to manage our inventory properly, we fail to release new products on schedule, or for any other reason, then our revenue for that quarter could fall below our expectations or those of securities analysts and investors, resulting in a decline in our stock price.

We rely on third party channel partners to generate a significant portion, and to fulfill a substantial majority, of our revenue, and if we fail to expand and manage our distribution channels, our revenues could decline and our growth prospects could suffer.

Historically our channel partners have originated more than 40%, and fulfilled approximately 85%, of our sales, and we expect that channel sales will represent a substantial portion of our revenues for the foreseeable future. Our ability to expand our distribution channels depends in part on our ability to educate our channel partners about our products and services, which are complex. Our agreements with our channel partners are generally non-exclusive and many of our channel partners have more established relationships with our competitors. If our channel partners choose to place greater emphasis on products and services of their own or those offered by our competitors, our ability to grow our business and sell our products may be adversely affected. If our channel partners do not effectively market and sell our products and services, or if they fail to meet the needs of our customers, then our ability to grow our business and sell our products may be adversely affected. The loss of one or more of our larger channel partners, who may cease marketing our products with limited or no notice, and our possible inability to replace them could adversely affect our sales. Our failure to recruit additional channel partners, or any reduction or delay in their sales of our products and services or conflicts between channel sales and our direct sales and marketing activities could materially and adversely affect our results of operations.

We face intense competition, especially from larger, better-known companies and we may lack sufficient financial or other resources to maintain or improve our competitive position.

The market for data center security products is intensely competitive and we expect competition to intensify in the future. Our competitors include companies such as Akamai Technologies, Inc., Citrix Systems, Inc., F5 Networks, Inc., International Business Machines Corporation (IBM), McAfee, Inc., Oracle Corporation, Symantec Corporation and other point solution security vendors.

Many of our existing and potential competitors may have substantial competitive advantages such as:

- greater name recognition and longer operating histories;
- larger sales and marketing budgets and resources and the capacity to leverage their sales efforts and marketing expenditures across a broader portfolio of products;
- broader, deeper or otherwise more well-established relationships with customers and potential customers;
- broader distribution networks and more established relationships with distributors;
- wider geographic presence;
- access to larger customer bases;
- greater customer support resources;
- greater resources to make acquisitions;
- greater resources to develop and introduce products that compete with our products;
- lower labor and development costs; and
- substantially greater financial, technical and other resources.

As a result, they may be able to adapt more quickly and effectively to new or emerging technologies and changing opportunities, standards or customer requirements. In addition, these companies could reduce the price of their competing products, resulting in intensified pricing pressures within our market. Further, some of our larger competitors have substantially broader product offerings and leverage their relationships based on other products or

incorporate functionality into existing products in a manner that discourages customers from purchasing our products. Our competitors may offer a bundled product offering, and our customers may elect to accept this offering from our competitors, even if it has more limited functionality than our product offering, instead of adding the additional appliances required to implement our offering. The consolidation in our industry, such as IBM s acquisition of Guardium, Inc., Oracle s acquisition of Secerno, Ltd. and McAfee s acquisition of Sentrigo, Inc., increases the likelihood of competition based on integration or bundling, particularly where their products and offerings are effectively integrated, and we believe that consolidation in our industry may increase the competitive pressures we face on all our products. If we are unable to sufficiently differentiate our products from the integrated or bundled products of our competitors, such as by offering enhanced functionality, performance or value, we may see a decrease in demand for those products, which would adversely affect our business, operating results and financial condition. Further, it is possible that continued industry consolidation may impact customers perceptions of the viability of smaller or even medium-sized software firms and consequently customers willingness to purchase from such firms. Similarly, if customers seek to concentrate their software purchases in the product portfolios of a few large providers, we may be at a competitive disadvantage notwithstanding the superior performance that we believe our products can deliver. Larger competitors are also often in a better position to withstand any significant reduction in capital spending by customers, and will therefore not be as susceptible to economic downturns.

Also, many of our smaller competitors that specialize in providing protection from a single type of business security threat may deliver these specialized business security products to the market more quickly than we can or may introduce innovative new products or enhancements before we do. Conditions in our markets could change rapidly and significantly as a result of technological advancements.

We may not compete successfully against our current or potential competitors. Companies competing with us may introduce products that have greater performance or functionality, are easier to implement or use, or incorporate technological advances that we have not yet developed or implemented. Our current and potential competitors may also establish cooperative relationships among themselves or with third parties that may further enhance their resources. In addition, companies competing with us may price their products more competitively than ours, or have an entirely different pricing or distribution model. Increased competition could result in fewer customer orders, price reductions, reduced operating margins and loss of market share. Further, we may be required to make substantial additional investments in research, development, marketing and sales in order to respond to competition, and we cannot assure you that we will be able to compete successfully in the future.

We operate in an evolving market that has not yet reached widespread adoption and where new or existing technologies that may be perceived to address the risks in different ways could gain wide adoption and supplant some or all of our products and services, making analysis of trends or predictions about our business difficult and potentially weakening our sales and our financial results.

We are in a new, rapidly evolving category in the security industry that focuses on securing our customers high-value business data. We offer database, file and web application security in an integrated, modular business security solution. Because we depend in part on the market s acceptance of our products and customers may choose to acquire technologies that are not directly comparable to ours, it is difficult to evaluate trends that may affect our business, including how large the business security market will be and what products customers will adopt. For example, organizations that use other security products, such as network firewalls, security

information and event management (SIEM) products or data loss prevention (DLP) solutions, may believe that these security solutions sufficiently protect access to sensitive data. Therefore, they may continue spending their IT security budgets on these products and may not adopt our business security solutions in addition to such products. If customers do not recognize the benefit our business security solution offers in addition to other security products, then our revenue may not grow quickly or may decline, and our stock price could decline.

The introduction of products and services embodying new technologies could render some or all of our existing products and services obsolete or less attractive to customers. Other business security technologies exist or could be developed in the future, and our business could be materially negatively affected if such technologies are widely adopted. We may not be able to successfully anticipate or adapt to changing technology or customer requirements on a timely basis, or at all. Currently less than 30% of our customers have purchased more than one of our product families. Even if customers purchase our products, they may not make repeat purchases or purchase other elements of our SecureSphere Business Security Suite, which may be exacerbated by the rapid evolution of our market. If we are unable to entice customers to buy products from multiple product families, then our revenue may not grow quickly or may decline, and our stock price could decline. If we fail to keep up with technological changes or to convince our customers and potential customers of the value of our solutions even in light of new technologies, our business, financial condition and results of operations could be materially and adversely affected.

In addition, because of our rapidly evolving market, any predictions about our future revenue may not be as accurate as they would be if we operated in a more established market.

If we do not successfully anticipate market needs and opportunities or changes in the legal, regulatory and industry standard landscape and make timely enhancements to our products and develop new products that meet those needs, we may not be able to compete effectively and our ability to generate revenues will suffer.

The business security market is characterized by rapid technological advances, changes in customer requirements, including customer requirements driven by changes to legal, regulatory and self-regulatory compliance mandates, frequent new product introductions and enhancements and evolving industry standards in computer hardware and software technology. Customers and industry analysts expect speedy introduction of software and new functionality to respond to new threats, requirements and risks and we may be unable to meet these expectations. As a result, we must continually change and improve our products in response to changes in operating systems, application software, computer and communications hardware, networking software, data center architectures, programming tools and computer language technology. Moreover, the technology in our products is especially complex because it needs to effectively identify and respond to methods of attack and theft, while minimizing the impact on database, file system and web application performance. In addition, our products must successfully interoperate with products from other vendors.

We cannot guarantee that we will be able to anticipate future market needs and opportunities or be able to develop product enhancements or new products to meet such needs or opportunities in a timely manner or at all. Since developing new products or new versions of, or add-ons to, existing products is complex, the timetable for their commercial release is difficult to predict and may vary from our historical experience, which could result in delays in their introduction from anticipated or announced release dates. We may not offer updates as rapidly as new threats affect our customers or our newly developed products or enhancements may have defects, errors or failures. If we do not quickly respond to the rapidly changing and rigorous needs of our customers by developing and introducing on a timely basis new and effective products, upgrades and services that can respond adequately to new security threats, it our competitive position, business and growth prospects will be harmed.

Even if we are able to anticipate, develop and commercially introduce enhancements and new products, there can be no assurance that we will be successful in developing sufficient market awareness of them or that such enhancements or new products will achieve widespread market acceptance. For example, while the majority of our current revenues are derived from the sales of our SecureSphere appliances, we are now offering cloud-based business security services through Incapsula and Skyfence. The market for cloud-based business security solutions is relatively new and it is uncertain whether Incapsula s and Skyfence s services will gain market acceptance. In addition, diversifying our product offerings will require significant investment and planning, will bring us more directly into competition with software providers that may be better established or have greater resources than we do, will require additional investment of time and resources in the development and training of our channel and strategic partners and will entail a significant risk of failure.

Further, one factor that drives demand for our products and services is the legal, regulatory and industry standard framework in which our customers operate, and we expect that will continue for the foreseeable future. For example, many of our customers purchase our web application security products to help them comply with the security standards developed and maintained by the Payment Card Industry (PCI) Security Standards Council (the PCI Council), which apply to companies that process or store credit card information. Laws, regulations and industry standards are subject to drastic changes that, particularly in the case of industry standards, may arrive with little or no notice, and these could either help or hurt the demand for our products. If we are unable to adapt our products and services to changing regulatory standards in a timely manner, or if our products fail to expedite our customers compliance initiatives, our customers may lose confidence in our products and could switch to products offered by our competitors. In

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addition, if regulations and standards related to business security are changed in a manner that makes them less onerous, our customers may view government and industry regulatory compliance as less critical to their businesses, and our customers may be less willing to purchase our products and services. In either case, our sales and financial results would suffer.

Real or perceived errors, failures or bugs in our products, particularly those that result in our customers experiencing security breaches, could adversely affect our reputation and business could be harmed.

Our products and services are very complex and have contained and may contain undetected defects or errors, especially when first introduced or when new versions are released. Defects in our products may impede or block network traffic or cause our products or services to fail to help secure high-value business data. Defects in our products may lead to product returns and require us to implement design changes or software updates.

Any defects or errors in our products, or the perception of such defects or errors, could result in:

- expenditure of significant financial and product development resources in efforts to analyze, correct, eliminate or work around errors or defects;
- loss of existing or potential customers or channel partners;
- delayed or lost revenue;
- delay or failure to attain market acceptance;
- delay in the development or release of new products or services;
- negative publicity, which will harm our reputation;
- warranty claims against us, which could result in an increase in our provision for doubtful accounts;
- an increase in collection cycles for accounts receivable or the expense and risk of litigation; and
- harm to our results of operations.

Data thieves are sophisticated, often affiliated with organized crime and operate large scale and complex automated attacks. In addition, their techniques change frequently and generally are not recognized until launched against a target. If we fail to identify and respond to new and complex methods of attack and to update our products to detect or prevent such threats in time to protect our customers high-value business data, our business and reputation will suffer.

In addition, many of our end-user customers use our products in applications that are critical to their businesses and may have a greater sensitivity to defects in our products than to defects in other, less critical, software products. An actual or perceived security breach or theft of the sensitive data of one of our customers, regardless of whether the breach is attributable to the failure of our products or services, could adversely affect the market s perception of our security products. Despite our best efforts, there is no guarantee that our products will be free of flaws or vulnerabilities, and even if we discover these weaknesses we may not be able to correct them promptly, if at all. Our customers may also misuse our products, which could result in a breach or theft of business data.

Although we have limitation of liability provisions in our standard terms and conditions of sale, they may not fully or effectively protect us from claims as a result of federal, state or local laws or ordinances or unfavorable judicial decisions in the United States or other countries. The sale and support of our products also entail the risk of product liability claims. We maintain insurance to protect against certain claims associated with the use of our products, but our insurance coverage may not adequately cover all claims asserted against us. In addition, even claims that ultimately are unsuccessful could result in our expenditure of funds in litigation and divert management s time and other resources.

False detection of security breaches or false identification of malicious sources could adversely affect our business.

Our business security products may falsely detect threats that do not actually exist. For example, our ThreatRadar product relies on information on attack sources aggregated from third-party data providers who monitor global malicious activity originating from anonymous proxies, specific IP addresses, botnets and phishing sites. If the information from these data providers is inaccurate, the potential for false positives increases. These false positives, while typical in the industry, may impair the perceived reliability of our products and may therefore adversely impact market acceptance of our products. If our products and services restrict access to important databases, files or applications based on falsely identifying users or traffic as an attack or otherwise unauthorized, this could adversely affect customers businesses. Any such false identification of users or traffic could result in negative publicity, loss of customers and sales, increased costs to remedy any problem and costly litigation.

Our success in acquiring and integrating other businesses, products or technologies could impact our financial position.

In order to remain competitive, we may seek to acquire additional businesses, products or technologies, any of which could be material to our business, operating results and financial condition. For example, we acquired assets from Tomium Software, LLC in January 2014, acquired Skyfence Networks Ltd. in February 2014 and acquired the remaining portion of Incapsula that we did not

already own in March 2014. The environment for acquisitions in the markets in which we operate is very competitive and acquisition candidate purchase prices will likely exceed what we would prefer to pay, but may be required to pay in order to make an acquisition. Furthermore, we may not find suitable acquisition candidates, and acquisitions we complete may not be successfully integrated in our overall business. Achieving the anticipated benefits of future acquisitions will depend in part upon whether we can integrate acquired operations, products and technology in a timely and cost-effective manner.

Acquisitions involve many risks, including the following:

- an acquisition may negatively impact our results of operations because it:
  - may require us to incur charges and substantial debt or liabilities,
  - may cause adverse tax consequences, substantial depreciation or deferred compensation charges,
  - may result in acquired in-process research and development expenses or in the future may require the amortization, write-down or impairment of amounts related to deferred compensation, goodwill and other intangible assets, or
  - may not generate sufficient financial return to offset acquisition costs;
- we may encounter difficulties or unforeseen expenditures in integrating the business, technologies, products, personnel or operations of any company that we acquire, particularly if key personnel of the acquired company decide not to work for us;
- an acquisition and integration process is complex, expensive and time consuming, and may disrupt our ongoing business, divert resources, increase our expenses and distract our management;
- an acquisition may result in a delay or reduction of customer purchases for both us and the company acquired due to customer uncertainty about continuity and effectiveness of service from either company;
- we may encounter difficulties in, or may be unable to, successfully sell any acquired products; and
- we may obtain unanticipated or unknown liabilities or become exposed to unanticipated risks in connection with any acquisition;

an acquisition may involve the entry into geographic or business markets in which we have little or no prior experience.

If we are unable to effectively execute acquisitions, our business, financial condition and results of operations could be adversely affected.

Delays or interruptions in the manufacturing and delivery of SecureSphere appliances by our sole source manufacturer may harm our business.

Our hardware appliances are built by a single manufacturer. Our reliance on a sole manufacturer, particularly a foreign manufacturer, involves several risks, including a potential inability to obtain an adequate supply of appliances and limited control over pricing, quality and timely delivery of products. In addition, replacing this manufacturer may be difficult and could result in an inability or delay in obtaining products. As a result, we may be unable to fulfill customer orders and our operating results may fluctuate from period to period, particularly if a disruption occurs near the end of a fiscal period.

Our manufacturer s ability to timely manufacture and ship our appliances in large quantities depends on a variety of factors. The manufacturer relies on a limited number of sources for the supply of functional components, such as semiconductors, printed circuit boards and hard disk drives. Functional component supply shortages or delays could prevent or delay the manufacture and shipment of appliances and, in the event of shortages or delays, we may not be able to procure alternative functional components on similar pricing terms, if at all. In addition, contractual restrictions or claims for infringement of intellectual property rights may restrict our manufacturer s use of certain components. These restrictions or claims may require our manufacturer to utilize alternative components or obtain additional licenses or technologies, and may impede its ability to manufacture and deliver appliances on a timely or cost-effective basis. If at some point, the manufacturer is no longer financially viable, we may lose our source of supply with little or no notice or recourse. Further, even if quality products are timely manufactured, delays in shipping may occur, resulting in delayed satisfaction of a primary revenue recognition criterion.

In the event of an interruption from this manufacturer, we may not be able to develop alternate or secondary sources in a timely manner. If we are unable to buy our appliances in quantities sufficient to meet our requirements, we will not be able to deliver products to our channel partners and customers, which would seriously affect present and future sales.

A failure to manage excess inventories or inventory shortages could result in decreased revenue and gross margins and harm our business.

We purchase products from our manufacturing partner outside of and in advance of reseller or customer orders and hold products in inventory. If we fail to accurately predict demand and as a result our manufacturer maintains insufficient hardware inventory or excess inventory, we may be unable to timely deliver ordered products or may have substantial inventory expense. Because our channel partners do not purchase our products in advance of customer orders, we may face additional difficulty in accurately forecasting demand for our hardware products. There is a risk we may forecast incorrectly and may be unable to sell excess

products ordered from our manufacturing partner. Inventory levels in excess of customer demand may result in inventory write-downs, and the sale of excess inventory at discounted prices could significantly impair our brand image and have an adverse effect on our financial condition and results of operations.

Conversely, if we underestimate demand for our products or if our manufacturing partner fails to supply products we require at the time we need them, we may experience inventory shortages. Inventory shortages might delay shipments to resellers, distributors and customers or cause us to lose sales. Further, as the size of individual orders increases, the risk that we may be unable to deliver unforecasted orders also increases, particularly near the end of quarterly periods. These shortages may diminish the loyalty of our channel partners or customers.

The difficulty in forecasting demand also makes it difficult to estimate our future financial condition and results of operations from period to period. A failure to accurately predict the level of demand for our products could adversely affect our net revenues and net income, and we are unlikely to forecast such effects with any certainty in advance.

We have operations outside of the United States and a significant portion of our customers and suppliers are located outside of the United States, which subjects us to a number of risks associated with conducting international operations.

We market and sell our products throughout the world and have personnel in many parts of the world. In addition, we have sales offices and research and development facilities outside the United States and we conduct, and expect to continue to conduct, a significant amount of our business with companies that are located outside the United States, particularly in Israel, Asia and Europe. We also source our components for our products from various geographical regions and ship components from a foreign production facility. Therefore, we are subject to risks associated with having international sales and worldwide operations, including:

- challenges caused by distance, language, cultural differences and the competitive environment;
- multiple and conflicting laws and regulations, including complications due to unexpected changes in these laws and regulations;
- trade and foreign exchange restrictions;
- foreign currency exchange fluctuations and foreign exchange controls;
- economic, social or political instability in foreign markets;
- greater difficulty in enforcing contracts, accounts receivable collection and longer collection periods;
- changes in regulatory requirements;

- difficulties and costs of staffing and managing foreign operations or relationships with channel partners;

- the uncertainty and limitation of protection for intellectual property rights in some countries;

- costs of complying with U.S. and foreign laws and regulations, including import and export control laws, tariffs, trade barriers, economic sanctions and other regulatory or contractual limitations on our ability to sell our products in certain foreign markets, and the risks and costs of non-compliance or complaints of non-compliance;

- heightened risks of unfair or corrupt business practices, actual or claimed, in certain geographies and of improper or fraudulent sales arrangements that may impact financial results and result in restatements of, and irregularities in, financial statements;

- the potential that our operations in the U.S. may limit the acceptability of our products to some foreign governments, and vice versa;

- the potential for acts of terrorism, hostilities or war;

- management communication and integration problems resulting from cultural differences and geographic dispersion; and

- multiple and possibly overlapping tax structures.

Our product and service sales may be subject to foreign governmental regulations, which vary substantially from country to country and change from time to time. Failure to comply with these regulations could adversely affect our business. Violations of laws or key control policies by our employees, contractors, channel partners or agents could result in delays in revenue recognition, financial reporting misstatements, fines, penalties or the prohibition of the importation or exportation of our products and services and could have a material adverse effect on our business and results of operations.

A portion of our revenue is generated by sales to government entities and such sales are subject to a number of challenges and risks.

Sales to U.S. and foreign federal, state and local governmental agency customers have accounted for approximately 12% of our bookings in the year ended December 31, 2011, 11% of our bookings for the year ended December 31, 2012, 13% of our bookings for the year ended December 31 2013 and 14% of our bookings for the six months ended June 30, 2014, and we may in the future increase sales to government entities. Sales into government entities are subject to a number of risks. Selling to government entities can be highly competitive, expensive and time consuming, often requiring significant upfront time and expense without any assurance that we will complete a sale. Accordingly:

changes in fiscal or contracting policies or decreases and uncertainties in available government funding, including as a result of the recent sequestration by the U.S. federal government and the recent partial shutdown of the U.S. federal government and any future recurrence of either event;

changes in government programs or applicable requirements;

the adoption of new laws or regulations or changes to existing laws or regulations;

changes in political or social attitudes with respect to security issues; and

potential delays or changes in the government appropriations process, including actions such as spending freezes implemented to address political or fiscal policy concerns,

could cause governments and governmental agencies to delay or refrain from purchasing the products and services that we offer in the future or otherwise have an adverse effect on our business, financial condition and results of operations.

Most of our sales to government entities have been made indirectly through our channel partners. Government entities may have contractual or other legal rights to terminate contracts with our distributors and resellers for convenience or due to a default, and any such termination may adversely impact our results of operations.

In addition, for purchases by the U.S. federal government, we must comply with laws and regulations relating to U.S. federal government contracting, which affect how we and our channel partners do business in connection with U.S. federal agencies. These laws and regulations may impose added costs on our business, and failure to comply with these or other applicable regulations and requirements, including non-compliance in the past, could lead to claims for damages from our channel partners, penalties, termination of contracts and suspension or debarment from government contracting for a period of time. Any such damages, penalties, disruption or limitation in our ability to do business with the U.S. federal government may adversely impact our results of operations.

Our business in countries with a history of corruption and transactions with foreign governments increase the risks associated with our international activities.

As we operate and sell internationally, we are subject to the U.S. Foreign Corrupt Practices Act, or the FCPA, and other laws that prohibit improper payments or offers of payments to foreign governments and their officials and political parties for the purpose of obtaining or retaining business. We have operations, deal with and make sales to governmental customers in countries known to experience corruption, particularly certain emerging countries in Africa, East Asia, Eastern Europe, South America and the Middle East. Our activities in these countries create the risk of unauthorized payments or offers of payments by one of our employees, consultants, sales agents or channel partners that could be in violation of various anti-corruption laws, even though these parties may not be under our control. While we have implemented safeguards to prevent these practices by our employees, consultants, sales agents and channel partners, our existing safeguards and any future improvements may prove to be less than effective, and our employees, consultants, sales agents or channel partners may engage in conduct for which we might be held responsible. Violations of the FCPA may result in severe criminal or civil sanctions, including suspension or debarment from U.S. government contracting, and we may be subject to other liabilities, which could negatively affect our business, operating results and financial condition.

We rely significantly on revenue from maintenance and support which may decline and, because we recognize revenue from such services over the term of the relevant service period, downturns or upturns in sales are not immediately reflected in full in our operating results.

Our maintenance and support revenue accounted for 31% of our total revenue for 2011, 32% of our total revenue for 2012, 32% of our total revenue for year ended December 31, 2013 and 37% of our total revenue for the six months ended June 30, 2014. Sales of new or renewal of such services contracts may decline or fluctuate as a result of a number of factors, including customers level of satisfaction with our products and services, the prices of our products and services, the prices of products and services offered by our competitors or reductions in our customers spending levels. If our sales of new or renewal services contracts decline, our revenue or revenue growth may decline and our business will suffer. In addition, we recognize service revenue ratably over the term of the relevant service period, which is typically one to three years but has been as long as five years. As a result, much of the revenue we report each quarter is the recognition of deferred revenue from services contracts entered into during previous quarters. Consequently, a decline in new or renewal services contracts in any one quarter will not be fully reflected in revenue in that quarter, but will negatively affect our revenue in future quarters. Accordingly, the effect of significant downturns in new or renewed sales of our services would not be reflected in full in our results of operations until future periods.

If we are unable to increase sales to larger customers, our results of operations may suffer.

We continuously seek to increase sales of our products to large enterprises, managed security service providers and government entities. Sales to large enterprises, service providers and government entities involve risks that may not be present, or are present to a lesser extent, with sales to small to mid-sized entities. These risks include:

- preexisting relationships with larger, entrenched providers of security solutions who have access to key decision makers within the organization and who also have the ability to bundle competing products with a broader product offering;

- increased purchasing power and leverage held by large customers in negotiating contractual arrangements with us;

- more stringent requirements in our support service contracts, including stricter support response times, and increased penalties for any failure to meet support requirements; and

- longer sales cycles, including lengthening of sales cycles due to competitive pressures or the evaluation by customers of both our cloud security solutions from Incapsula and our on-premise products as potential alternatives, and the associated risk that substantial time and resources may be spent on a potential customer who elects not to purchase our products and services.

In addition, product purchases by enterprises, managed security service providers, cloud hosting providers and government entities are frequently subject to budget constraints, multiple approvals, and unplanned administrative, processing and other delays. The ongoing general increase in the number of security vendors vying for mindshare, in some cases using overlapping or confusing messaging, may combine with these factors to extend the sales cycles for our products and services. Further, large enterprises, managed security service providers, cloud hosting providers and government entities typically have longer implementation cycles; require greater product functionality and scalability and a broader range of services; demand that vendors take on a larger share of risks; sometimes require acceptance provisions that can lead to a delay in revenue recognition; and expect greater payment flexibility from vendors. All these factors can add risk to doing business with these customers. If our sales expectations for a large customer do not materialize in a particular quarter or at all, then our business, financial condition and results of operations could be materially and adversely affected.

If our existing and potential customers migrate to hosted, cloud-based data centers that do not deploy our products, our revenues could suffer.

The majority of our current sales are made through a model in which our channel partners sell our business security solutions to large enterprise customers that operate their own data centers and have the ability to choose the business security solutions and configurations to fit their environment. If our large enterprise customers and potential customers choose to outsource the hosting of their data centers to large, multi-tenancy hosting providers like Rackspace Hosting, Inc. and Amazon.com, Inc., they may not be able to choose what business security solutions are deployed in these hosted environments, and our current sales model may not be effective. Although we work with large hosting services providers, like Rackspace Hosting, Inc. and Savvis, Inc., to integrate our business security solutions into their hosting environments so that our solutions may be offered to their hosting customers, we cannot guarantee that all such hosting service providers will adopt our solutions, offer them as a choice to their customers or promote our solutions over those of our competitors. Even if these large hosting services providers integrate our business security solutions into their hosting environments and promote our solutions, they may be able to negotiate larger discounts than individual enterprise customers and, consequently, the average selling price of our products may decrease and our revenue would suffer. Alternatively, they may offer services based on our competitors products at lower cost or bundled with other services that we do not offer, and their customers may choose those services even if they would otherwise chose our products if making a decision on a stand-alone basis.

If our customers are not satisfied with our technical support or professional services, they may choose not to purchase our products and services or to renew maintenance contracts, either of which would adversely impact our business and results of operations.

Our business relies on our customers satisfaction with the technical support and professional consulting services we provide to support our products. If we fail to provide technical support services that are responsive, satisfy our customers expectations and resolve issues that they encounter with our products and services, then they may elect not to purchase or renew annual maintenance and support contracts and they may choose not to purchase additional products and services from us. Accordingly, our failure to provide satisfactory technical support or professional services could have a material and adverse effect on our business and results of operations.

We are exposed to fluctuations in currency exchange rates, which could negatively affect our financial condition and results of operations.

Our functional and reporting currency is the U.S. dollar and we generate a majority of our revenue in U.S. dollars. However, in 2011, 2012, 2013 and the six months ended June 30, 2014, we incurred approximately 37%, 41%, 37% and 35%, respectively, of our expenses outside of the United States in foreign currencies, primarily the Israeli shekel, principally with respect to salaries and related personnel expenses associated with our Israeli operations. The exchange rate between the U.S. dollar and foreign currencies has fluctuated substantially in recent years and may continue to fluctuate substantially in the future. We expect that a majority of our revenues will continue to be generated in U.S. dollars for the foreseeable future and that a significant portion of our expenses, including personnel costs, as well as capital and operating expenditures, will continue to be denominated in Israeli shekels. The results of our operations may be adversely affected by foreign exchange fluctuations.

We use forward foreign exchange contracts to hedge or mitigate the effect of changes in foreign exchange rates on our operating expenses denominated in certain foreign currencies. However, this strategy might not eliminate our exposure to foreign exchange rate fluctuations and involves costs and risks of its own, such as cash expenditures, ongoing management time and expertise, external costs to implement the strategy and potential accounting implications. Additionally, our hedging activities may contribute to increased losses as a result of volatility in foreign currency markets.

Our business and operations have experienced rapid growth, and if we do not appropriately manage any future growth, or are unable to improve our systems and processes, our operating results will be negatively affected.

We have experienced rapid growth over the last several years. For example, we grew from 383 employees as of December 31, 2011, to 474 employees as of December 31, 2012, to 580 employees as of December 31, 2013 and then to 715 employees as of June 30, 2014. This growth has placed, and will continue to place, a strain on our employees, management systems and other resources. Managing our growth will require significant expenditures and allocation of valuable management resources. We rely heavily on information technology systems to help manage critical functions, such as order processing, revenue recognition, financial forecasts and inventory and supply chain management. To manage any future growth effectively, we must continue to improve our information technology and financial infrastructure, operating and administrative systems and controls, and continue to manage headcount, capital and processes in an efficient manner. We may not be able to successfully implement improvements to these systems and processes in a timely manner.

In addition, we rely heavily on hosted, Software-as-a-Service (SaaS) technologies from third parties in order to operate critical functions of our business, including ERP services from NetSuite and customer relationship management (CRM) services from salesforce.com, inc. If these services become unavailable due to extended outages or interruptions or because they are no longer available on commercially reasonable terms or prices, our expenses could increase, our ability to manage our finances could be interrupted and our processes for managing sales of our products and services and supporting our customers could be impaired until equivalent services, if available, are identified, obtained and integrated; all of which could harm our business.

Also, our systems and processes may not prevent or detect all errors, omissions or fraud. Our failure to improve our systems and processes, or their failure to operate in the intended manner, may result in our inability to manage the growth of our business and to accurately forecast our revenue, expenses and earnings, or to prevent certain losses. Our productivity and the quality of our products and services may also be adversely affected if we do not integrate and train our new employees quickly and effectively. Any future growth would add complexity to our organization and require effective coordination across our organization. If we fail to achieve the necessary level of efficiency in our organization as it grows or otherwise fail to manage any future growth effectively, we could incur increased costs, and experience a loss of customer and investor confidence in our internal systems and processes, any of which could result in harm to our business, results of operations and financial condition.

Assertions by third parties of infringement or other violations by us of their intellectual property rights could result in significant costs and substantially harm our business and operating results.

Patent and other intellectual property disputes are common in the IT security industry. Some companies in the IT security industry, including some of our competitors, own large numbers of patents, copyrights, trademarks and trade secrets, which they may use to assert claims against us. This disparity between our patent portfolio and the patent portfolios of our most significant competitors may increase the risk that they may sue us for patent infringement and may limit our ability to counterclaim for patent infringement or settle through patent cross-licenses. In addition, there are also patent holding companies or other patent owners who are solely or primarily in the business of building

portfolios of patents and asserting them against operating companies, often with little merit, and who have no relevant product revenues and against whom potential assertions our patents (and potential patents) may provide little or no deterrence. Third parties have asserted and may in the future assert claims of infringement, misappropriation or other violations of intellectual property rights against us. For example, in May 2010, F5 Networks, Inc., an IT infrastructure company that competes with us in the web application firewall market, filed a lawsuit against us alleging patent infringement. In June 2010, we filed a counterclaim alleging patent infringement by F5 Networks, Inc. In February 2011, we entered into a settlement and license agreement with F5 Networks, Inc., which dismissed the litigation. Third parties may also assert such claims against our customers or channel partners whom we typically indemnify against claims that our products infringe, misappropriate or otherwise violate the intellectual property rights of third parties. As the numbers of products and competitors in our market increase and overlaps occur, claims of infringement, misappropriation and other violations of intellectual property rights may increase. Also, to the extent we hire personnel from competitors, we may be subject to allegations that they have been improperly solicited or have divulged proprietary or other confidential information.

We cannot assure you that we are not infringing or otherwise violating any third-party intellectual property rights. Further, any claim of infringement, misappropriation or other violation of intellectual property rights by a third party, even those without merit, could be asserted against us, cause us to incur substantial costs defending against the claim and could distract our management from our business. An adverse outcome of a dispute may require us to pay substantial damages, including treble damages, if we are found to have willfully infringed a third party s patents or copyrights; cease making, licensing or using solutions that are alleged to infringe or misappropriate the intellectual property of others; expend additional development resources to attempt to redesign our products or services or otherwise to develop non-infringing technology, which may not be successful; enter into potentially unfavorable royalty or license agreements in order to obtain the right to use necessary technologies or intellectual property rights; and indemnify our

customers and partners. Royalty or licensing agreements, if required or desirable, may be unavailable on terms acceptable to us, or at all, or may require significant royalty payments and other expenditures. In addition, some licenses may be non-exclusive, and therefore our competitors may have access to the same technology licensed to us. Any of these events could seriously harm our business, financial condition and results of operations.

We rely on the availability of licenses to third-party software and other intellectual property, the loss of which could increase our costs and delay software shipments.

Many of our products and services include software or other intellectual property licensed from third parties, and we also use software and other intellectual property licensed from third parties in our business. This exposes us to risks over which we may have little or no control. For example, a licensor may have errors or defects in its products that harm our business, may have difficulties keeping up with technological changes or may stop supporting the software or other intellectual property that it licenses to us. Also, it will be necessary in the future to renew licenses, expand the scope of existing licenses or seek new licenses, relating to various aspects of these products and services, or otherwise relating to our business, which may result in increased license fees. In addition, a direct or indirect licensor may assert that we or our customers are in breach of the terms of a license, which could, among other things, give such licensor the right to terminate a license or seek damages from us, or both. Moreover, the inclusion in our products and services of software or other intellectual property licensed from third parties on a nonexclusive basis could limit our ability to differentiate our products from those of our competitors.

Licensed software may not continue to be available on commercially reasonable terms, or at all. While we believe that there are currently adequate replacements for third-party software, any loss of the right to use any of this software could result in delays in producing or delivering our software until equivalent technology is identified and integrated, which delays could harm our business. Our business would be disrupted if any of the software we license from others or functional equivalents of this software were either no longer available to us or no longer offered to us on commercially reasonable terms. In either case, we would be required to either redesign our products to function with software available from other parties or to develop these components ourselves, which would result in increased costs and could result in delays in our product shipments and the release of new product offerings. Furthermore, we might be forced to limit the features available in our current or future products. If we fail to maintain or renegotiate any of these software licenses, we could face significant delays and diversion of resources in attempting to license and integrate a functional equivalent of the software. Any of these events could have a material adverse effect on our business, financial condition and results of operations.

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

Certain of our products are distributed with software licensed under open source licenses. Some of these licenses contain requirements that we make available source code for modifications or derivative works we create based upon the open source software, and that we license these modifications or derivative works under the terms of a particular open source license or subject to certain license requirements. If we combine our proprietary software with open source software in a certain manner, we could, under certain provisions of the open source licenses, be required to release the source code of our proprietary software. In addition to risks related to license requirements, usage of open source software can subject us to greater risks than use of third-party commercial software, as licensors of open source software generally do not provide warranties or any indemnification for infringement of third party intellectual property rights. We have established processes to help alleviate these risks, including a review process for screening requests from our development organization for the use of open source software, but we cannot be sure that all open source software is submitted for approval prior to use in our products. In addition, open source license terms may be ambiguous and many of the risks associated with use of open source software cannot be eliminated, and could, if not

properly addressed, negatively affect our business. If we were found to have inappropriately used open source software, we might be required to re-engineer our products, to release proprietary source code, to discontinue the sale of our products in the event re-engineering could not be accomplished on a timely basis or to take other remedial action that may divert resources away from our development efforts, any of which could adversely affect our business, operating results and financial condition. Disclosing the source code of our proprietary software could make it easier for malicious third parties to discover vulnerabilities in our business security products and allow our competitors to create similar products with decreased development effort and time. Any of these events could have a material adverse effect on our reputation, business, financial condition and results of operations.

Failure to protect our proprietary technology and intellectual property rights could substantially harm our business and operating results.

Our success depends, in part, on our ability to protect proprietary methods and technologies that we develop under the intellectual property laws of the United States and other countries, so that we can prevent others from using our inventions and proprietary information. We attempt to protect our intellectual property under patent, trademark, copyright and trade secret laws, and through a combination of confidentiality procedures, contractual provisions and other methods, all of which offer only limited protection. If we fail to protect our intellectual property rights adequately, our competitors might gain access to our technology, and our business might be harmed. In addition, defending our intellectual property rights might entail significant expenses. Any of our patents, copyrights, trademarks or other intellectual property rights may be challenged by others or invalidated through administrative process or litigation. We have 13 issued patents and 11 patent applications pending as of August 1, 2014 in the United States. Our issued patents, which are limited in number compared to some of our competitors, may not provide us with any competitive advantages or may be challenged by third parties, and our patent applications may never be granted at all. Additionally, the process of obtaining patent protection is expensive and time-consuming, and we may not be able to prosecute all necessary or desirable patent applications at a reasonable cost or in a timely manner. Further, for strategic and other reasons we may choose not to seek patent protection for certain innovations and may choose not to pursue patent protection in certain jurisdictions. Even if issued, there can be no assurance that our patents will adequately protect our intellectual property, as the legal standards relating to the validity, enforceability and scope of protection of patent and other intellectual property rights are uncertain.

Any patents that are issued may subsequently be invalidated or otherwise limited, enabling other companies to better develop products that compete with ours, which could adversely affect our competitive business position, business prospects and financial condition. In addition, issuance of a patent does not guarantee that we have a right to practice the patented invention. Patent applications in the U.S. are typically not published until 18 months after filing, or in some cases not at all, and publications of discoveries in industry-related literature lag behind actual discoveries. We cannot be certain that we were the first to make the inventions claimed in our issued patents or pending patent applications or otherwise used in our products, that we were the first to file for protection in our patent applications, or that third parties do not have blocking patents that could be used to prevent us from marketing or practicing our patented products or technology. Effective patent, trademark, copyright and trade secret protection may not be available to us in every country in which our products and services are available. The laws of some foreign countries may not be as protective of intellectual property rights as those in the United States, and mechanisms for enforcement of intellectual property rights may be inadequate. Accordingly, despite our efforts, we may be unable to prevent third parties from infringing upon or misappropriating our intellectual property.

We might be required to spend significant resources to monitor and protect our intellectual property rights. We may initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. Any litigation, whether or not it is resolved in our favor, could result in significant expense to us and divert the efforts of our technical and management personnel, which may adversely affect our business, operating results and financial condition.

We may become subject to claims for remuneration or royalties for assigned service invention rights by our Israeli employees, which could result in litigation and adversely affect our business.

We have entered into assignment of invention agreements with our Israeli employees pursuant to which such individuals agree to assign to us all rights to any inventions created in the scope of their employment or engagement with us. A significant portion of our intellectual property has been developed by our Israeli employees in the course of their employment for us. Under the Israeli Patents Law, 5727-1967, or the Patents Law, inventions conceived by an employee during the scope of his or her employment with a company are regarded as service inventions, which belong to the employer, absent a specific agreement between the employee and employer giving the employee service invention rights. The Patents Law also provides that if there is no such agreement between an employer and an employee, the Israeli Compensation and Royalties Committee, or the Committee, a body constituted under the Patents Law, shall determine whether the employee is entitled to remuneration for his or her inventions. Recent decisions by the Committee have created uncertainty in this area, as it held that employees may be entitled to remuneration for their service inventions despite having specifically waived any such rights. Further, the Committee has not yet determined the method for calculating this Committee-enforced remuneration. Although our Israeli employees have agreed to assign to us service invention rights, we may face claims demanding remuneration in consideration for assigned inventions. As a consequence of such claims, we could be required to pay additional remuneration or royalties to our current and/or former Israeli employees, or be forced to litigate such claims, which could negatively affect our business.

Confidentiality agreements with partners, employees, consultants and others may not adequately prevent disclosure of trade secrets and other proprietary information.

In order to protect our proprietary technology, processes and methods, we rely in part on confidentiality agreements and other restrictions with our customers, partners, employees, consultants and others. These agreements may not effectively prevent disclosure of confidential information and may not provide an adequate remedy in the event of unauthorized disclosure of confidential information. Despite our efforts to protect our proprietary technology, processes and methods, unauthorized parties may attempt to misappropriate, reverse engineer or otherwise obtain and

use them. We may be unable to determine the extent of any unauthorized use or infringement of our products, technologies or intellectual property rights. In addition, others may independently develop identical or substantially similar technology and in these cases we would not be able to assert any trade secret rights against those parties. Moreover, policing unauthorized use of our technologies, products and intellectual property is difficult, expensive and time-consuming, particularly in foreign countries where the laws may not be as protective of intellectual property rights as those in the United States and where mechanisms for enforcement of intellectual property rights may be weak. Costly and time-consuming litigation could be necessary to enforce and determine the scope of our proprietary rights, and failure to obtain or maintain trade secret protection could adversely affect our competitive business position.

Conditions in Israel may limit our ability to develop and sell our products. This could result in a decline in revenues.

Our principal research and development facilities are located in Israel. Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its neighboring countries, as well as incidents of civil unrest, and a number of state and non-state actors have publicly committed to its destruction. Political, economic and military conditions in Israel could directly affect our operations. We could be adversely affected by any major hostilities involving Israel, including acts of terrorism or any other hostilities involving or threatening Israel, the interruption or curtailment of trade between Israel and its trading partners, a significant increase in inflation or a significant downturn in the economic or financial condition of Israel. Any on-going or

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future violence between Israel and the Palestinians, including a continued escalation of the recent conflict in Gaza, armed conflicts, terrorist activities, tension along the Israeli borders or with other countries in the region, including Iran, or political instability in the region could disrupt international trading activities in Israel and may materially and negatively affect our business and could harm our results of operations.

Certain countries, as well as certain companies and organizations, continue to participate in a boycott of Israeli firms, firms with large Israeli operations and others doing business with Israel and Israeli companies. In addition, such boycott, restrictive laws, policies or practices may change over time in unpredictable ways, and could, individually or in the aggregate, have a material adverse effect on our business in the future.

Some of our employees in Israel, including one of our executive officers, are obligated to perform annual military reserve duty in the Israel Defense Forces, depending on their age and position in the armed forces. Furthermore, they may be called to active reserve duty at any time under emergency circumstances for extended periods of time. For example, in 2013, approximately 57 of our employees in Israel were called for active reserve duty, each serving for an average of approximately two weeks. Our operations could be disrupted by the absence, for a significant period, of one or more of our executive officers or key employees due to military service, and any significant disruption in our operations could harm our business.

If we are unable to hire, retain and motivate qualified personnel, our business would suffer.

We depend on the continued contributions of our senior management and other key employees to execute on our business plan, and to identify and pursue new opportunities and product innovations. The loss of services of senior management or other key employees, particularly Shlomo Kramer, one of our founders and our President and Chief Executive Officer; Amichai Shulman, one of our founders and our Chief Technology Officer; and Terrence J. Schmid, our Chief Financial Officer and Treasurer, could significantly delay or prevent the achievement of our development and strategic objectives.

Our future success depends, in part, on our ability to continue to attract and retain highly skilled technical, managerial, finance and other personnel, particularly in our sales and marketing, research and development and professional service departments. Any of our employees may terminate their employment at any time. Competition for highly skilled personnel is frequently intense, globally for sales personnel, as well as in the San Francisco Bay Area and in Tel Aviv, Israel, the locations in which we have a substantial presence and need for highly-skilled personnel. We may be unable to attract and retain suitably qualified individuals who are capable of meeting our growing technical, operational and managerial requirements, on a timely basis or at all, and we may be required to pay increased compensation in order to do so. If we are unable to attract and retain the qualified personnel we need to succeed, our business will suffer.

Volatility or lack of performance in our stock price may also affect our ability to attract and retain our key employees. Employees may be more likely to leave us if the shares or restricted stock units they hold have declined in value or if the exercise prices of the options that they hold are significantly below the market price of our common stock. If we are unable to retain our employees, our business, operating results and financial condition will be harmed.

Our internal network system and website may be subject to intentional disruption that could adversely impact our reputation and future sales.

Because we are a leading provider of business security products, hackers and others may try to access our data or compromise our systems. Similarly, experienced computer programmers may attempt to penetrate our network security or the security of our website and cause interruptions of our services. Because the techniques used by such

computer programmers to access or sabotage networks change frequently and may not be recognized until launched against a target, we may be unable to anticipate these techniques. The theft and/or unauthorized use or publication of our trade secrets and other confidential business information as a result of such an event could adversely affect our competitive position, reputation, brand and future sales of our products, and could impair our ability to operate our business, including our ability to provide subscription or maintenance and support services to our customers. We could suffer monetary and other losses and reputational harm in the event of such incidents.

Outages, interruptions or delays in hosting services could impair the delivery of our cloud-based security services and harm our business.

We operate infrastructure that supports our ThreatRadar and Security Operations Center (SOC) services and use third party hosting facilities for certain ThreatRadar services. Despite precautions taken within our own internal network and at these third party facilities, the occurrence of a natural disaster or an act of terrorism or other unanticipated problems could result in lengthy interruptions in our services.

The cloud-based security services that we provide through our majority-owned subsidiary, Incapsula, are operated from a network of third party facilities that host the software and systems that operate these security services. Any damage to, or failure of, our internal systems or systems at third party hosting facilities could result in outages or interruptions in our cloud-based services. Outages or interruptions in our cloud-based security services may cause our customers and potential customers to believe our cloud-based security services are unreliable, cause us to issue credits or pay penalties, cause customers to terminate their subscriptions and adversely affect our renewal rates and our ability to attract new customers, ultimately harming our business and revenue.

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We are subject to governmental export and import controls that could subject us to liability or impair our ability to compete in international markets.

Our products incorporate encryption technology and may be exported outside the U.S. only if we obtain an export license or qualify for an export license exception. Compliance with applicable regulatory requirements regarding the export of our products may prevent our customers with international operations from deploying our products throughout their global systems or, in some cases, prevent the export of our products to some countries altogether. Further, various countries regulate the import of encryption technology and appliance-based products and have enacted laws that could limit our ability to distribute products, could create delays in the introduction of our products in those countries or could limit our customers ability to implement our products in those countries. Any new export or import restrictions, new legislation or shifting approaches in the enforcement or scope of existing regulations, or in the countries, persons or technologies targeted by such regulations, could result in decreased use of our products by existing customers with international operations, declining adoption of our products by new customers with international operations and decreased revenues. If we, or our channel partners, fail to comply with export and import regulations, we may be denied export privileges, be subjected to fines or other penalties, be unable to sell our products in certain countries and we may potentially suffer reputational harm.

Furthermore, U.S. export control laws and economic sanctions prohibit the shipment of certain products to U.S. embargoed or sanctioned countries, governments and persons. While we take precautions to prevent our product from being shipped to U.S. sanctions targets, our products could be shipped to those targets by our channel partners despite our efforts. Any such shipment could have negative consequences including government investigations, penalties and reputational harm. Any change in economic sanctions or related legislation, shift in the enforcement or scope of existing regulations, or change in the countries, governments, persons or technologies targeted by such regulations, could result in decreased use of our products by, or in our decreased ability to export or sell our products to, existing or potential customers with international operations. Any limitation on our ability to export or sell our products would likely adversely affect our business, financial condition and results of operations.

Changes in our provision for income taxes or adverse outcomes resulting from examination of our income tax returns could adversely affect our results.

We are subject to income taxation in the United States and numerous foreign jurisdictions. Determining our provision for income taxes requires significant management judgment. In addition, our provision for income taxes is subject to volatility and could be adversely affected by many factors, including, among other things, changes to our operating or holding structure, changes in the amounts of earnings in jurisdictions with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities and changes in tax laws. We are subject to ongoing tax examinations in various jurisdictions. Tax authorities may disagree with our intercompany charges, cross-jurisdictional transfer pricing or other matters and assess additional taxes. While we regularly assess the likely outcomes of these examinations to determine the adequacy of our provision for income taxes, there can be no assurance that the outcomes of such examinations will not have a material impact on our operating results and cash flows.

Significant judgment is required to determine the recognition and measurement attributes prescribed in Accounting Standards Codification (ASC) 740-25 (formerly referred to as Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109). In addition, ASC 740-25 applies to all income tax positions, including the potential recovery of previously paid taxes, which if settled unfavorably could adversely impact our provision for income taxes or additional paid-in capital. In addition, we are subject to the continuous examination of our income tax returns by the U.S. Internal Revenue Service and other tax authorities. We regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. There can be no assurance that the outcomes from these continuous examinations will

not have an adverse effect on our results of operations.

Our business is subject to the risks of earthquakes, fire, power outages, floods and other catastrophic events, and to interruption by manmade problems such as terrorism.

A significant natural disaster, such as an earthquake, fire or a flood, or a significant power outage could have a material adverse impact on our business, financial condition and results of operations. Our corporate headquarters are located in the San Francisco Bay Area, a region known for seismic activity, on land reclaimed from the bay that is susceptible to high liquefaction risk in the event of an earthquake. In addition, natural disasters could affect our manufacturing vendors or logistics providers ability to perform services such as manufacturing products on a timely basis and assisting with shipments on a timely basis. In the event our service providers information technology systems or manufacturing or logistics abilities are hindered by any of the events discussed above, shipments could be delayed, resulting in missing financial targets, such as revenue and shipment targets, for a particular quarter. Further, if a natural disaster occurs in a region from which we derive a significant portion of our revenue, customers in that region may delay or forego purchases of our products, which may materially and adversely impact our results of operations for a particular period. In addition, acts of terrorism could cause disruptions in our business or the business of our manufacturer, logistics providers, partners, customers or the economy as a whole. Given our typical concentration of sales at each quarter end, any disruption in the business of our manufacturer, logistics providers, partners or customers that impacts sales at the end of our quarter could have a significant adverse impact on our quarterly results. All of the aforementioned risks may be augmented if the business continuity plans for us and our suppliers prove to be inadequate. To the extent that any of the above results in delays or cancellations of customer orders, or the delay in the manufacture, deployment or shipment of our products, our business, financial condition and results of operations would be adversely affected.

Risks Related to Ownership of our Common Stock

Market volatility may affect our stock price and the value of your investment

The trading prices of the securities of technology companies have been highly volatile. The market price of our common stock may fluctuate significantly in response to a number of factors, most of which we cannot predict or control, including:

- announcements of new products, services or technologies, commercial relationships, acquisitions, strategic partnerships, joint ventures, capital commitments or other events by us or our competitors;
- fluctuations in operating performance and in stock market prices and trading volumes of securities of other technology companies generally, or those in our industry in particular;
- general market conditions and overall price and volume fluctuations in U.S. equity markets;
- actual or anticipated variations in our operating results, or the operating results of our competitors;
- the financial and other projections we may provide to the public, any changes in these projections or our failure to meet these projections or changes in our financial guidance or securities analysts estimates of our financial performance;
- failure of securities analysts to maintain coverage of us, changes in financial or other estimates by any securities analysts who follow us, or our failure to meet these estimates or the expectations of our investors;
- ratings or other changes by any securities analysts who follow our company or our industry;
- sales of large blocks of our common stock, including sales by our executive officers, directors and significant stockholders;
- rumors and market speculation involving Imperva or other companies in our industry; and
- lawsuits threatened or filed against us and changing legal or regulatory developments in the United States and other countries.

In addition, the stock market in general, and the New York Stock Exchange in particular, have experienced substantial price and volume volatility that is often seemingly unrelated to the operating performance of particular companies. These broad market fluctuations or factors affecting us more specifically may cause the trading price of our common

stock to decline. In the past, securities class action litigation has often been brought against a company after a period of volatility in the market price of its common stock.

We face risks related to securities litigation that could result in significant legal expenses and settlement or damage awards.

We are currently and may in the future become subject to claims and litigation alleging violations of the securities laws or similar claims, which could harm our business and require us to incur significant costs. For example, on April 11, 2014, a purported stockholder class action lawsuit was filed in the United States District Court for the Northern District of California against Imperva and certain of its officers alleging that defendants made false and misleading statements and purporting to assert claims for violations of the federal securities laws, and seeking unspecified compensatory damages and other relief. In addition, on June 27, 2014, Imperva (as a nominal defendant) was named in purported derivative litigation filed in the Court of Chancery in the State of Delaware. Regardless of the outcome, these matters or future litigation may require significant attention from management and could result in significant legal expenses, settlement costs or damage awards that could have a material impact on our financial position, results of operations and cash flows.

If we fail to maintain an effective system of disclosure controls and procedures and internal controls over financial reporting, our ability to produce accurate financial statements or comply with applicable regulations could be impaired.

As a public company, we are subject to the reporting requirements of the Exchange Act, the Sarbanes-Oxley Act of 2002 (the Sarbanes-Oxley Act), and the rules and regulations of the New York Stock Exchange. We expect that the requirements of these rules and regulations will continue to increase our legal, accounting and financial compliance costs, make some activities more difficult, time-consuming and costly and place strains on our personnel, systems and resources.

The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal control over financial reporting. We are continuing to develop and refine our disclosure controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file with the SEC is recorded, processed, summarized and reported within the time periods specified in SEC s rules and forms. Our current controls and any new controls that we develop may become inadequate because of changes in conditions, and the degree of compliance with the policies or procedures may deteriorate. In addition, weaknesses in our internal controls over financial reporting may be discovered in the future. Our filings with the SEC are subject to periodic review by the SEC, and our auditors are subject to periodic inspection by the Public Company Accounting Oversight Board (PCAOB). Any failure to maintain effective controls over financial reporting, any difficulties encountered in the implementation of additional controls or the improvement of existing controls, or any issues that emerge as a result of regulatory review, could harm our operating results or cause us to fail to meet our reporting obligations and may result in a revision

or restatement of our prior period financial statements. Any failure to maintain effective internal controls also could adversely affect the results of periodic management evaluations and annual independent registered public accounting firm attestation reports regarding the effectiveness of our internal control over financial reporting that we are required to include in our annual reports filed with the SEC under Section 404 of the Sarbanes-Oxley Act. Ineffective disclosure controls and procedures and internal control over financial reporting could also cause investors to lose confidence in our reported financial and other information, which would likely have a negative effect on the trading price of our common stock.

In order to maintain and improve the effectiveness of our disclosure controls and procedures and internal control over financial reporting, we have expended, and anticipate that we will continue to expend, significant resources and provide significant management oversight, which involve substantial accounting-related costs. Any failure to maintain the adequacy of our internal controls, or consequent inability to produce accurate financial statements on a timely basis, could increase our operating costs and could materially impair our ability to operate our business. In the event that we are not able to continue to demonstrate compliance with Section 404 of the Sarbanes-Oxley Act in a timely manner, that our internal controls are perceived as inadequate or that we are unable to produce timely or accurate financial statements, investors may lose confidence in our operating results and our stock price could decline. In addition, if we are unable to continue to meet these requirements, we may not be able to remain listed on the New York Stock Exchange.

We also have implemented elements of a disaster recovery/business continuity plan for our accounting and related information technology systems but we have not yet implemented a complete disaster recovery/business continuity plan. If the elements that we have developed and plan to develop in the future prove inadequate in the circumstances of a particular disaster or other business continuity event our ability to maintain timely accounting and reporting may be materially impaired.

If securities or industry analysts do not publish research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.

The trading market for our common stock will depend in part on the research and reports that securities or industry analysts publish about us or our industry. If we do not establish and maintain adequate research coverage or if one or more of the analysts who covers us downgrades our stock or publishes inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analysts ceases coverage of our company or fails to publish reports on us regularly, demand for our stock could decrease, which could cause our stock price and trading volume to decline.

We do not intend to pay dividends on our common stock so any returns will be limited to the value of our stock.

We have never declared or paid any cash dividend on our common stock. We currently anticipate that we will retain future earnings for the development, operation and expansion of our business and do not anticipate declaring or paying any cash dividends for the foreseeable future. Any return to stockholders will therefore be limited to the value of their stock.

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of us, which may be beneficial to our stockholders, more difficult and may prevent attempts by our stockholders to replace or remove our current management.

Provisions in our restated certificate of incorporation and amended and restated bylaws may delay or prevent an acquisition of us or a change in our management. These provisions include:

authorizing blank check preferred stock, which could be issued by the board without stockholder approval and may contain voting, liquidation, dividend and other rights superior to our common stock, which would increase the number of outstanding shares and could thwart a takeover attempt;

a classified board of directors whose members can be dismissed only for cause;

the prohibition on actions by written consent of our stockholders;

the limitation on who may call a special meeting of stockholders;

the establishment of advance notice requirements for nominations for election to our board of directors or for proposing matters that can be acted upon at stockholder meetings; and

the requirement of at least 75% of the outstanding capital stock to amend any of the foregoing second through fifth provisions.

In addition, because we are incorporated in Delaware, we are governed by the provisions of the anti-takeover provisions of the Delaware General Corporation Law, which may discourage, delay or prevent a change in control by prohibiting us from engaging in a business combination with an interested stockholder for a period of three years after the person becomes an interested stockholder, even if a change of control would be beneficial to our existing stockholders. Although we believe these provisions collectively provide for an opportunity to obtain greater value for stockholders by requiring potential acquirers to negotiate with our board of directors, they would apply even if an offer rejected by our board were considered beneficial by some stockholders. In addition, these provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management.

Our ability to use our net operating loss carryforwards may be subject to limitations and may result in increased future tax liability to us.

Generally, a change of more than 50% in the ownership of a corporation s stock, by value, over a three-year period constitutes an ownership change for U.S. federal income tax purposes. An ownership change may limit a company s ability to use its net operating loss carryforwards attributable to the period prior to such change. We have not performed a detailed analysis to determine whether an ownership change under Section 382 of the Internal Revenue Code has occurred after each of our previous private placements of preferred stock or after the issuance of shares of common stock in connection with our initial public offering. In the event we have undergone an ownership change under Section 382, if we earn net taxable income, our ability to use our pre-change net operating loss carryforwards to offset U.S. federal taxable income may become subject to limitations, which could potentially result in increased future tax liability to us.

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

Use of Proceeds from Public Offering of Common Stock

The Form S-1 Registration Statement (Registration No. 333-175008) relating to our IPO was declared effective by the SEC on November 8, 2011, and the offering of our common stock commenced on November 9, 2011. J.P. Morgan Securities LLC and Deutsche Bank Securities Inc. acted as joint book-running managers for the offering, and RBC Capital Markets, LLC, Lazard Capital Markets LLC and Pacific Crest Securities, Inc. acted as co-managers of the offering. The offering of 5,000,000 shares of our common stock has been completed.

The net proceeds to us of our IPO after deducting $6.9 million of underwriters discounts and $5.8 million of offering expenses were $86.2 million. In January 2012, we invested $3.5 million of the net proceeds to us resulting from our IPO in Incapsula, our majority owned subsidiary, and received in exchange an additional 4,375,000 shares of Incapsula s Series A-1 Preferred Stock. In October 2013, we loaned $1.1 million of the net IPO proceeds to Incapsula at a rate of 2% per annum with a maturity date of December 31, 2014. In January 2014, we paid approximately $4.7 million in cash as part of the consideration in connection with our purchase of certain assets and liabilities of Tomium Software, LLC. In February 2014, we paid $8.6 million in cash, in addition to a holdback payment commitment due 24 months from the acquisition close valued at approximately $7.2 million, as part of the consideration in connection with the acquisition of SkyFence Networks Ltd. We expect to use remaining net IPO proceeds for working capital and general corporate purposes, including acquisitions. Although we may also use a portion of the net proceeds for acquisition of complementary businesses, technologies or other assets, we have no present understandings, commitments or agreements to enter into any acquisitions other than the acquisition of the outstanding securities of Incapsula not already owned by Imperva.

Our management will retain broad discretion in the allocation and use of the net proceeds of our IPO, and investors will be relying on the judgment of our management regarding the application of the net proceeds. Pending specific utilization of the net proceeds as described above, we have invested the net proceeds of the offering in short-term, interest-bearing obligations. The goal with respect to the investment of the net proceeds will be capital preservation and liquidity so that such funds are readily available to fund our operations.

Unregistered Sales of Equity Securities

For the quarter ended June 30, 2014, we did not sell any unregistered securities.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

See Exhibit Index.

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SIGNATURES

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

Date: August 8, 2014

IMPERVA, INC.

By: /s/ Shlomo Kramer
Shlomo Kramer
President and Chief Executive Officer

(Principal Executive Officer)

Date: August 8, 2014

By: /s/ Terrence J. Schmid
Terrence J. Schmid
Chief Financial Officer

(Principal Financial Officer)

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EXHIBIT INDEX

Exhibit Number	Exhibit Description
10.01+	Third Amendment to OEM Agreement dated as of May 22, 2014 among Imperva, Inc., Imperva, Ltd. and American Portwell Technology.
31.01	Certification of Principal Executive Officer Pursuant to Securities Exchange Act Rule 13a-14(a).
31.02	Certification of Principal Financial Officer Pursuant to Securities Exchange Act Rule 13a-14(a).
32.01*	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350 and Securities Exchange Act Rule 13a-14(b).
32.02*	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350 and Securities Exchange Act Rule 13a-14(b).
101.INS**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema Document
101.CAL**	XBRL Taxonomy Calculation Linkbase Document
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB**	XBRL Taxonomy Label Linkbase Document
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document

+ Certain portions of this exhibit have been omitted and have been filed separately with the SEC pursuant to a request for confidential treatment under Rule 24b-2 as promulgated under the Securities Exchange Act of 1934, as amended.

* This certification is not deemed filed for purposes of Section 18 of the Securities Exchange Act, or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that Imperva Inc. specifically incorporates it by reference.

** These exhibits are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.